No. 10,062

In the United States Circuit Court of Appeals

For the Ninth Circuit

THE BANK OF CALIFORNIA, NATIONAL ASSOCIATION,

Appellant,

vs.

GEORGE M. McBRIDE, Trustee of Western Bond & Mortgage Company, a corporation, Bankrupt,

Appellee.

BRIEF OF APPELLEE

Upon Appeal from the District Court of the United States for the District of Oregon.

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CODES, STATUTES AND RULES

TEXTBOOK

HISTORY OF THE PROCEEDINGS

SUMMARY PROCEEDINGS BEFORE REFEREE CANNON

The Trustee in Bankruptcy herein on July 16, 1936, filed a petition for an order against the Bank of California requiring it to turn over to the Trustee property of the Bankrupt which it had acquired after the filing of the petition in bankruptcy, namely: certain real property known as the Russell Ranch in Oregon, and certain Bonds, which petition was thereafter amended (Tr. 18-30). The order to show cause was issued and the Bank of California challenged the jurisdiction of the Court to hear such matter summarily (Tr. 35-38). The Referee, upon said challenge, determined that the Court had summary jurisdiction (Tr. 38-45). Thereupon, the Bank filed its answer to the petition and to the order to show cause, wherein it renewed its challenge to the jurisdiction and maintained its right to hold the property it had acquired (Tr. 45-58).

REFEREE CANNON'S FINDINGS AND ORDER

After hearing, the Referee filed his opinion, wherein he concluded "that the Bank must by order be required in some manner to restore the assets attempted to be destroyed by the instruments filed . . . . on March 2, 1932, ... and an order to this effect may be settled on service and notice" (Tr. 58-69). Thereupon, detailed findings and conclusions were filed (Tr. 69-83) and an order made (Tr. 83-89). The order directed the Bank to deed to the Trustee the Russell Ranch and to turn over the bonds. It further gave the Bank the option, within

ten days from the date of the order, in lieu of turning over the Ranch, to pay to the Trustee $65,000.00, the determined value of the Ranch, and $1,000.00, the determined value of the bonds, with interest from the date of acquisition by the Bank.

REVIEW OF REFEREE CANNON'S FINDINGS

Petition for review of this order was filed by the Bank (Tr. 90-95). Judge Fee, in an opinion filed February 27, 1939 (Tr. 106-110), determined that the Referee's findings were correct and should be affirmed, and likewise that the Referee's order should be approved with the exception of the optional right given to the Bank to pay money in lieu of property.

JUDGE FEE'S ORDER OF MAY 1, 1939

Judge Fee in an order made May 1, 1939, affirmed all of the Referee's findings (Tr. 111-112) and re-referred the matter to the Referee for the purpose of determining what, if any, allowance should be made for expenditures by the Bank upon the property, since the Bank in Paragraph XIII of its answer claimed to have expended certain moneys for improving the ranch property (Tr. 55-56). In view of the fact that Referee Cannon's term had expired, the matter was referred for such purpose to Referee Estes Snedecor, his successor. (Tr. 104-106).

PROCEEDINGS ON REFERENCE TO REFEREE SNEDECOR

Before Referee Snedecor the Bank attempted to introduce evidence "tending to show that the bankrupt received, directly or indirectly, a part of the consideration paid by the Bank to the Massachusetts Mortgage Co. for the assignment of the mort-

gages on the Russell Ranch." The Referee excluded this evidence, since he construed the order as confining "the limits of the present inquiry to such facts not found by the former findings" (Tr. 116-117). The former Referee had found that the Western had received nothing.

REFEREE SNEDECOR'S FINDINGS

After hearing the evidence introduced, Referee Snedecor found (Tr. 112-145) that the Bank was not entitled to any allowance for so-called improvements made by it upon the property, since it was not a bona fide purchaser for value of the property, but that it was entitled to a credit, against the reasonable rental value of the Ranch, for taxes paid by the Bank which the Trustee would have been obligated to pay in any event, and also for certain rentals paid by the Bank on outside lands for grazing purposes. These taxes and rentals aggregated $9,546.38. Referee Snedecor found the reasonable rental value of the Russell Ranch during its occupancy by the Bank, exclusive of the use of the permanent improvements made by it, to be $3000.00 per year, against which the $9,546.38 was to be credited. He also found that the Trustee was entitled to the sum of $10,000.00 which the Bank had received from the State Highway Commission for a right-of-way for highway purposes over said Ranch (Tr. 144).

HEARINGS BEFORE JUDGE FEE ON REFEREE SNEDECOR'S FINDINGS AND ON MOTION FOR REHEARING

Whereupon, the Trustee moved to confirm the findings of Referee Snedecor (Tr. 145-152) and the

Bank filed objections to said findings (Tr. 152-163). The Bank also filed at the same time a motion for rehearing of the findings made by Referee Cannon, approved on review by the Court in its order of May 1, 1939 (Tr. 164) based on newly discovered evidence (Tr. 164-172). Attached to said motion were affidavits referring to said so-called newly discovered evidence (Tr. 172-188). The motions and objections were heard by Judge Fee and on November 17, 1941, Judge Fee filed his opinion (Tr. 188-213), affirmed Referee Snedecor's findings, and refused to set aside his previous order affirming Referee Cannon's findings.

JUDGE FEE'S ORDER APPROVING REFEREE SNEDECOR'S FINDINGS, DENYING MOTION FOR REHEARING AND REFUSING TO SET ASIDE ORDER OF MAY 1, 1939.

Whereupon an order was entered overruling objections to the Referee's report and affirming and carrying into effect his recommendations (Tr. 222-227), and an order was likewise made upon the motion to rehear, refusing to set aside his order of May 1, 1939, which had affirmed the findings of Referee Cannon.

THE BANK'S APPEAL

The Bank of California thereupon appealed.

ISSUES FOR DECISION ON THIS APPEAL

Since the facts in this case have been passed upon by two Referees and approved and affirmed on review in each instance by District Judge Fee, and again reviewed by Judge Fee upon motion for re-

hearing, which motion he denied, it is confidently asserted that the facts in this six year long litigagation will not be re-examined except to discover if there were any evidence on which the findings were based (see Discussion pp. 27 to 30 this Brief and Appendix hereto). In view of the fact that the barest perusal of the evidence will speedily disclose that there was a plethora of testimony on which to base the findings, the only issues, therefore, for decision by this Court are those of law. They are:

(1) Did the Bankruptcy Court have summary jurisdiction to determine the controversy under the facts adduced?

(2) Having determined that the Bank of California had acquired the Bankrupt's property neither in good faith nor without notice, nor for a present consideration, did the Court properly disallow reimbursements to the Bank for asserted improvements?

However, we must perforce set forth the facts in this Brief since they have been inaccurately and misleadingly set forth under the heading "Statement of the Case" in Appellant's Brief (pp. 3-13). We shall call specific attention to particular misleading statements following our Statement of Facts.

STATEMENT OF THE FACTS

The Western Bond and Mortgage Company [1] was indebted to the Bank of California, N.A., in the

(1) For Brevity, the Western Bond and Mortgage Company will hereafter be demnoinated Western, and after the first mention hereafter of their respective names, the following companies will be referred to as follows: The Bank of California, N. A. as "Bank", Massachusetts Mortgage Co. as "Massachusetts", Keystone Finance Co. as "Keystone" and Ochoco Farms Corporation as "Ochoco".

amount of approximately $103,000.00.(1) During the year 1931 and prior to bankruptcy, the Bank procured collateral from the Western in the endeavor to protect in part this indebtedness (Tr. 362). Since such collateral was deemed insufficient to protect the Bank fully, it began to press the officers of the Western to obtain as far as possible a liquidation in full of the indebtedness (Tr. 361-2, 363). While this pressing process was in progress, there was filed on November 25, 1931, a petition in bankruptcy against the Western (Tr. 3-5). The Bank had knowledge of the filing of this petition (Tr. 252, 369, 370, and Trustee's Ex. 31).(2) After the filing of the petition, the Bank entered into negotiations (Tr. 262-263, 344, 362-363) with the Western through its new management (Tr. 262) under E. F. O'Flynn, then its Secretary-Treasurer (Tr. 300-1), and afterwards its President (Tr. 300), who was also head of the Massachusetts Mortgage Co. (Tr. 262, 369, also Ex. 30). This latter company owned all of the capital stock of the Western (Tr. 349, 369) and of the Ochoco Farms Corporation (Ex. 10, Tr. 255). The negotiations resulted in the Bank first crediting the Western's obligation with an amount equal to the value of the Western's collateral held (Tr. 336), and then by the Bank taking an assignment of a note for $55,960.00 (Tr. 337) secured by a first mortgage on the Russell Ranch (Tr. 338; Ex. 20,

(1) See admissions of Bank in Paragraph VII of its Answer to the Trustee's Petition for Order to Show Cause (Tr. 49).

(2) Exhibit 31 is the Credit file of the Bank on the Western. In it is a memo under date of Nov. 28, 1931, as follows: "11-28-31. Daily Journal of Commerce Western Bond and Mortgage Co.—Involuntary Petition in Bankruptcy B.D." Also, a communication or report from Bradstreet Company to the Bank of California dated Nov. 28, 1931, informing the Bank of the filing of the petition against the Western on Nov. 25, 1931.

Tr. 307), which the Bank caused to be appraised and found to be of a value of $65,000.00 (Tr. 386 and Ex. 30). Thereupon, the Bank gave to the Western a full release of indebtedness (Ex. 22, Tr. 309; Tr. 346, 396, 397). The amount owing the Bank plus certain advances made to the Massachusetts, less the value of the securities held which the Western assigned unconditionally to the Bank, was $55,960.00 (Tr. 337)—the exact amount of the assigned secured note.

The taking of the note for $55,960.00 and its obtaining of the mortgage securing the same, arose through the following circuitous method:

At the time of the bankruptcy, the Western was the owner of all the capital stock of the Keystone Finance Co. (Ex. 7, Tr. 277-8, 296-7). The officers and directors of the Keystone were women office employees and stenographers of the Western (Tr. 282-4, 292-295, 294, 298-303, 300). They admittedly did the bidding of the President of the Western, using no independent judgment (Tr. 283-4). They received no salary or other compensation from the Keystone (Tr. 302) and their entire compensation came from the Western (Tr. 302). They held only qualifying shares in the Keystone and owned no interest in such shares (Tr. 299). The Keystone's office, if it had one, was the office of the Western (Tr. 302), and it did not participate in paying for the same (Tr. 302).

Title to the Russell Ranch at the time of Bankruptcy was in the Keystone,[1] but the Western held

(1) See Paragraph II of Trustee's Petition for Order to Show Cause (Tr. 19-20) and Paragraph II of Answer of Bank to said Petition (Tr. 48).

two mortgages against it securing notes of the Keystone for $150,000.00[2]—an amount far in excess of its value (Tr. 386).

After the filing of the petition in bankruptcy against the Western, there was caused (Tr. 289) to be filed Articles of Incorporation of the Ochoco Farms Corporation. The Ochoco's officers and directors were the same stenographers and clerks of the Western who were officers of the Keystone, excepting that a Miss Thibodeaux, also a stenographer of the Western (Tr. 294), was substituted for Miss Smith. No incorporators', no stockholders', and no directors' meetings of the Ochoco were held (Tr. 287-8 and Ex. 12). No subscription to the stock was made (Tr. 286 and Ex. 12); no oath of Directors was taken (Tr. 288 and Ex. 12). The Ochoco had no bank account (Tr. 295); no business was ever transacted by it (Tr. 291). It paid no license fee to the State of Oregon, excepting that paid upon organization, and it was dissolved by action of the State for failing to pay such license fees (Tr. 292-3, Exs. 12A and 12B). The Keystone was then caused to give to Ochoco a deed to the Ranch. (Ex. 18, Tr. 305-6.)

The simulated character of the transactions is demonstrated by the fact that *five days prior to the incorporation of the Ochoco* (Ex. 9, Tr. 284), the Ochoco accepted the transfer of the Ranch property from the Keystone (Ex. 19, Tr. 306-7). No consideration was received for this transfer (Tr. 306, 341).

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(2) See admissions in Paragraph III of Answer of Bank to Trustee's Petition for Order to Show Cause (Tr. 48).

The officers signing the deed were E. E. Gallagher, President, and Miss B. O'Reilly, Assistant-Secretary (Tr. 305-6). Simultaneously and without consideration (Tr. 332-3; and see also Trustee's Exhibit 18-C under the Snedecor Hearing), the Western satisfied the first mortgages which it held upon the Ranch (Ex. 7, Tr. 305).

The next step taken was immediately to cause the Ochoco to execute and deliver to the Massachusetts a note of $55,960.00, secured by a mortgage on the Russell Ranch (Ex. 20, Tr. 307). The mortgage from Ochoco to Massachusetts was signed in the name of the Ochoco by E. E. Gallagher, President, and B. O'Reilly, Secretary, the same individuals who signed the deed from Keystone to Ochoco.

Then the Massachusetts, owning all the stock in the Western (Tr. 269), assigned to the Bank the note and mortgage given to it by the Ochoco.

The Bank had full knowledge of these circuitous transfers and transactions (see Ex. 30, Tr. 413), for its attorney held all the deeds, mortgages, satisfactions of mortgage, notes and assignments in escrow (Tr. 262-3, Ex. 22), and, upon the Bank satisfying itself that the property was worth $65,000.00, recorded all of them simultaneously (Tr. 260, 411). All of these instruments, including the deed of the Ranch to Ochoco were returned to the Bank's attorney (Tr. 411).

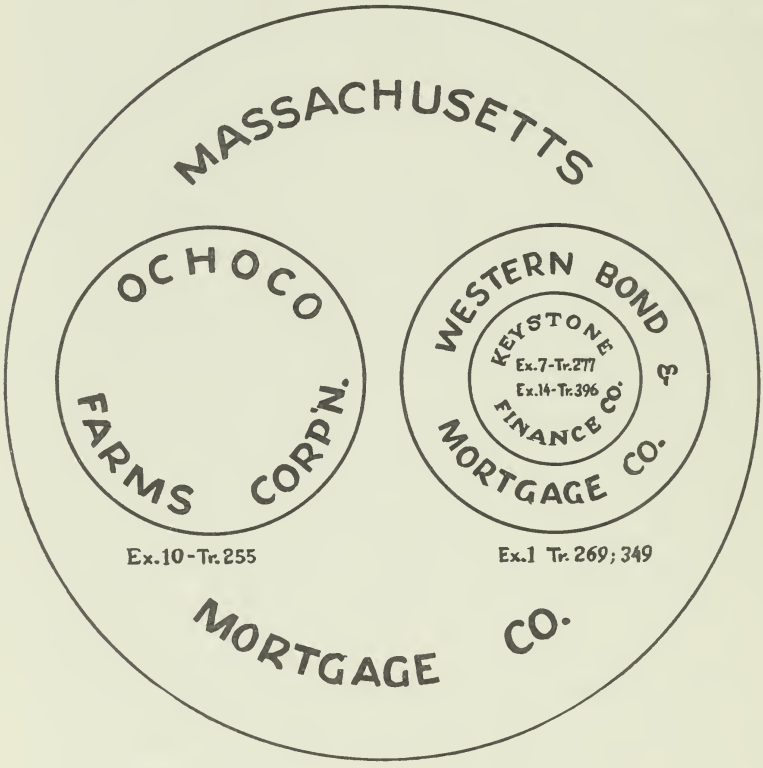
It is believed that the facts in this case can be grasped more readily and with less turning of pages if they are re-stated in succinct diagrammatic form. Accordingly, we present:

A DIAGRAMMATIC STATEMENT OF THE FACTS

DIAGRAM SHOWING

INTERLOCKING STOCK-OWNERSHIP IN VARIOUS CORPORATIONS INVOLVED,

WITH OVERALL COMPLETE OWNERSHIP IN MASSACHUSETTS.



INTERLOCKING OFFICES AND DIRECTORSHIPS OF WHAT JUDGE FEE DESIGNATED THE DRAMATIS PERSONAE OF THE VARIOUS CORPORATIONS (Tr. 190)

	Massachusetts Mortgage Co.	Western Bond & Mtg. Co.	Keystone Finance Co.	Ochoco Farms Corpn.
MR. E. F. O'FLYNN Directing Force	President (Tr. 369 Director (Tr. 369	Secty-Treas. (Tr. 281) President (Tr. 301) Director (Tr. 278)		
MISS E. E. GALLAGHER Stenographer of Western, owning no stock in any of the corporations, and holding merely qualifying share (Tr. 282-4, 294) and doing biddings of Western's President (Tr. 282-4, 292-5,300).	Director (Tr. 283)	Asst.-Treas. (Tr. 281) Director (Tr. 271, 281)	President (Tr. 298) Director (Tr. 298)	President (Tr. 293) Director (Tr. 293)
MISS LOUISE N. THIBEDEAUX Stenographer of Western, owning no stock in any of the corporations, holding merely qualifying share (Tr. 282-4) and doing business of Western's Pres. (Tr. 282-4, 292-5,300).	Director (Tr. 283)	Asst-Secty (Tr.281) Director (Tr. 281)	Secretary (Tr. 306)	Vice-Pres. (Tr. 294) Director (Tr. 293)
MISS B. O'REILLY Ditto			Vice-Pres. (Tr. 298) Director (Tr. 298)	Secty-Treas. (Tr. 294) Director (Tr. 293)

DIAGRAM SHOWING CIRCUITOUS TRANSFERS FROM WESTERN TO BANK

(ALL TRANSFERS OUT OF WESTERN WERE MADE AFTER BANKRUPTCY AND RECORDED SIMULTANEOUSLY BY BANK'S ATTORNEY - TR. 415)

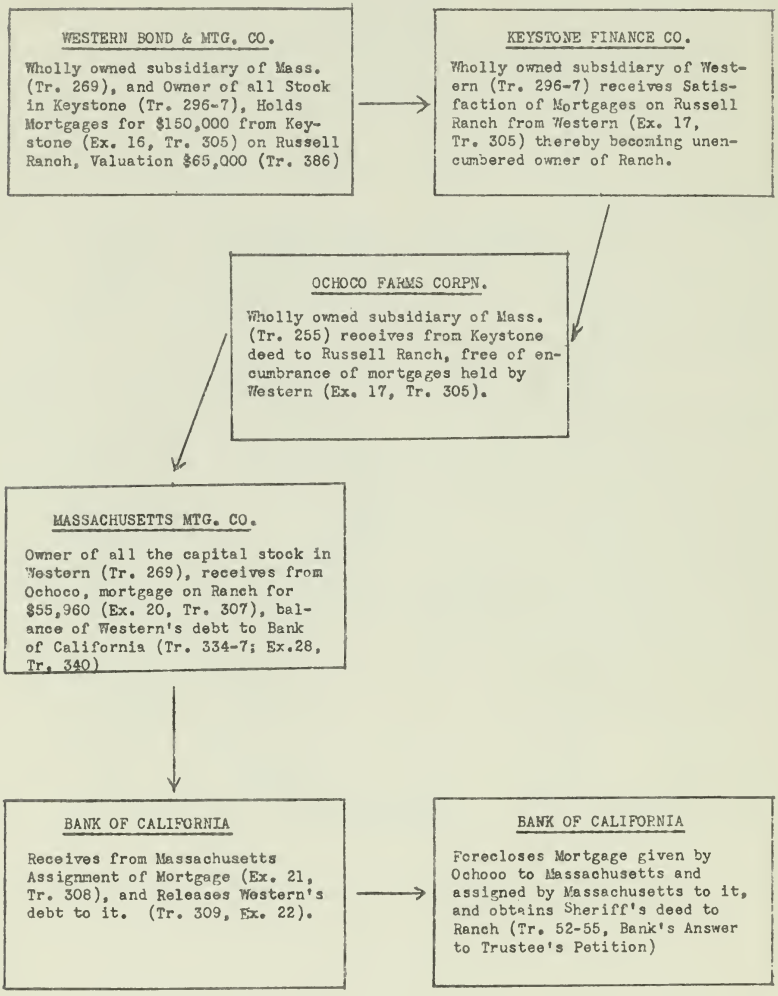


DIAGRAM OF SIMULATED CONSIDERATIONS FOR SATISFACTIONS, DEEDS, MORTGAGES AND ASSIGNMENTS OF MORTGAGES

WESTERN TO KEYSTONE

Satisfaction of Mortgages

Testimony shows that no consideration was received by the Western (Tr. 331-333)

↓

KEYSTONE TO OCHOCO

Deed

Keystone purported to have received 850 shares of the preferred stock of Western from Keystone (Tr. 306).

But, testimony shown owned no such shares (Tr. 340-1). And deed from Keystone (Ex. 18, Tr. 305-6) shows property conveyed to Ochoco five days before Ochoco was organized. (Tr. Ex. 9, Tr. 284, 289.)

↓

OCHOCO TO MASSACHUSETTS

Mortgage $55, 960

Purported Consideration: Need by Ochoco to Borrow Money (Ex. 12--Minute Book of Ochoco. Minutes of a purported directors' meeting held half hour before directors elected and signed by officers also half hour before they were elected.)

But, Ochoco never did any business (Tr. 291); never had a bank account (Tr. 295).

↓

MASSACHUSETTS TO BANK

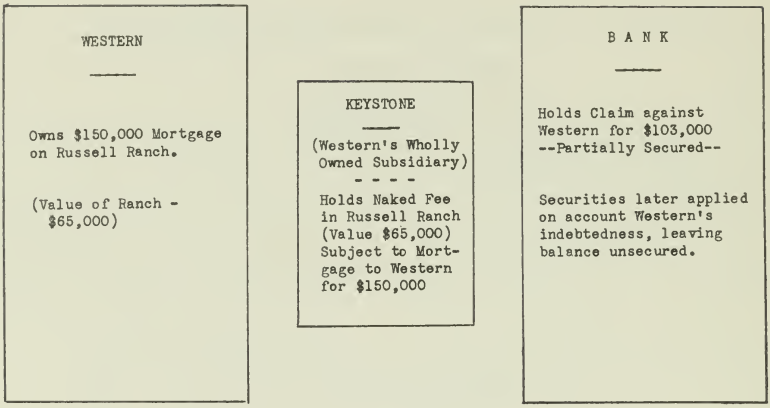
Assignment of Mortgage

Release of Western's debt to Bank.

But, debt released after bankruptcy (Tr. No present consideration.

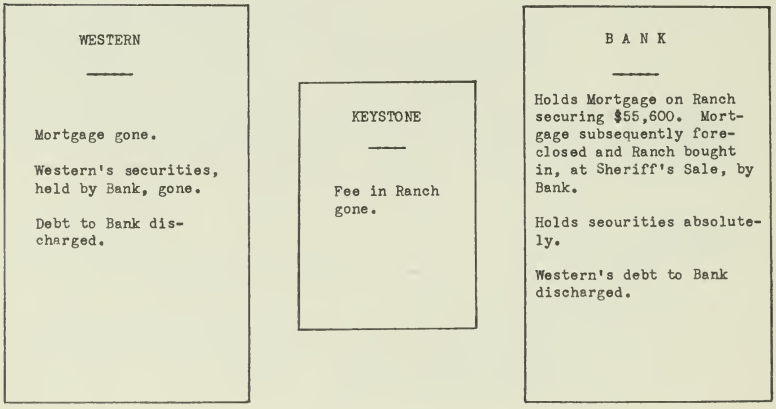
SITUATION OF PARTIES ON NOVEMBER 25, 1931

(AT DATE OF BANKRUPTCY - Tr. 204)



SITUATION OF PARTIES ON MARCH 2, 1932

(AFTER BANKRUPTCY AND AT DATE OF RECORDATION OF INSTRUMENTS BY BANK - Tr. 415)



MISSTATEMENT OF CASE IN APPELLANT'S BRIEF

As heretofore stated, the Appellant in its Brief presents an entirely erroneous factual picture of the case. Under guise of stating the facts in its "Statement of the Case" (pp. 3-13), it indulges (1) in many direct misstatements of fact, (2) in many statements of half facts, and (3) in many statements of fact based on rejected evidence. To such an extent are these elements injected in Appellant's "Statement of the Case", it is believed that that portion of its Brief will be disregarded by this Court. Some examples of each category, culled from many, are

(1) Misstatements of Fact

(a) "The Bank had no knowledge of the actual facts on which the Bankrupt later claimed its interest." (Appellant's Brief, p. 3)

The testimony showed that the Bank did have such knowledge, including actual knowledge of the filing of the petition in bankruptcy (see Note (2) p. 6 of this Brief). See also testimony of Thos. G. Greene, attorney for the Bank, in regard to his knowledge of the chain of title (Tr. 267). See statement of Thos. G. Greene, Tr. 369-370: "They (the Bank) had all the information I had."

(b) "A new corporation, Ochoco Farms Corporation, was formed, the stock of which was acquired by Massachusetts in exchange for 850 shares of the preferred stock of Western. These preferred shares were transferred by Ochoco to Keystone for title to the Russell Ranch." (Appellant's Brief p. 7)

The testimony showed that there were no such shares owned by the Massachusetts or by the Keystone (Tr. 340-341), so, of course, they could not have been transferred.

> (c) "On several other occasions he tried to question O'Flynn about the relations and transactions of the various companies of the Massachusetts Group." (App. Br. p. 8)

Mr. Greene in his testimony (Tr. 266) stated: "In fact I asked very little about it."

> (d) "The Bank dealt solely with O'Flynn as principal executive of the Massachusetts." (App. Br. p. 9)

O'Flynn was President of the Western, and there is no evidence in the record to show that the Bank dealt with O'Flynn solely in the one capacity.

> (e) "The Bank did not know what corporation owned the Russell Ranch before it was transferred to the Ochoco." (App. Br. p. 9)

The testimony is that Attorney Greene knew and Attorney Greene stated that the Bank actually knew all that he knew (Tr. 370).

> (f) "Attorney Greene's knowledge was limited to facts pertaining to the title and corporate resolutions." (App. Br. p. 9)

It is shown by Attorney Greene's testimony that before the subject of the transfer involving an examination of the title arose, Attorney Greene attended various trials brought against the Western in the state court and in the federal court and heard many charges made against the Western (Tr. 252, 256, 400, 406). He attended these trials "because the Bank of California was trying to get some *addi-*

tional security *from the Western Bond & Mortgage Company*" (Tr. 403). Moreover, prior to the request of the bank to have Mr. Greene examine the title, Mr. Greene had several interviews with Mr. O'Flynn, wherein Mr. O'Flynn made "various proposals to the Bank on behalf of the Massachusetts Mortgage Company as to what he was going to do in order to obtain discharge and release of the Bank of its claim *against the Western Bond & Mortgage Company*" (Tr. 262). Mr. Greene "suggested to him that pending the conclusion of the negotiations and the acceptance or rejection by the Bank of these *various* proposals that he had better leave the papers with me in escrow so there would be something besides chin music to rely upon" (Tr. 262). Mr. Greene further stated (Tr. 393): "I had seen the financial statement of the Western Bond & Mortgage Company and the financial statement of the Massachusetts Mortgage Company. . . . I had seen them before this matter was consummated." (Of course, Mr. Greene did not have to see statements of the Massachusetts or of the Western in order to pass on the title to the Russell Ranch.) So, it is obvious that the statement in Appellant's Brief that "Mr. Greene's knowledge was limited to facts pertaining to the title" is not a true statement of the evidence.

(g) "This line of reasoning raised important issues (a) whether the Keystone mortgage had any value and whether the debt it secured had not been paid, and (b) whether it actually was in possession of the bankrupt at the time the bankruptcy petition was filed.

"No evidence had been introduced with regard to either of these issues. There was no al-

legation in the petition with regard thereto, nor had the referee made any finding thereon." (App. Br. 11-12)

The record is replete with evidence as to these issues, and we merely refer to our analysis in the Appendix of this Brief. As to the allegations in the petition, we refer the Court to Paragraphs III and V, Tr. pp. 22 and 23, Paragraphs IX, X and XI, Tr. pp. 24-27, and Paragraph XIII, Tr. p. 28. As to the statement that the Referee made no findings in regard to said issues, we refer the Court to Finding No. 5, Tr. p. 73, and Finding No. 17 and No. 18, Tr. pp. 78-79.

(2) Half Facts

(a) "Keystone owned real property. Such a property was the Russell Ranch." (App. Br. 4)

The only piece of real property which was owned by the Keystone—if it actually owned that—was the Russell Ranch. The implication of the statement is that the Keystone owned other real property. There is no such evidence in the record and it is not a fact.

(b) "Keystone acquired the Russell Ranch on December 20, 1929, from Russell Land & Livestock Co. and mortgaged it to Western, to secure two notes for $72,500 and $77,500, respectively." (App. Br. 4)

The implication conveyed by this statement is that the Keystone purchased the Russell Ranch from a detached owner and that subsequently it was mortgaged to the Western . As a matter of fact, the property was transferred to the Keystone by a wholly owned subsidiary of the Western. The Rus-

sell Ranch and Livestock Company was in the same category as the Keystone. All the stock in each was wholly owned by the Western (Ex. 7, Tr. 277-8), and the Western simultaneously caused the Keystone to execute a mortgage thereon for a sum far in excess of its value.

> (c) "The Bank executives made a careful check as to the integrity and financial responsibility of Massachusetts and the reports which they received were extremely favorable. They acted on these and upon Mr. Greene's unqualified opinion as to the validity of the mortgage." (App. Br. 9)

As a matter of fact, the Bank made this investigation of the Massachusetts for the purpose of making to the Massachusetts a loan of $20 000.00 and took collateral from the Massachusetts to secure this loan. So, even had the contemplated deal not gone through, the Bank was well protected (Tr. 348-51). The loan was made before any report on the title was made by Mr. Greene (Tr. 336).

> (d) "In December, 1931, O'Flynn asked the Bank whether it would be interested in making a new loan to Massachusetts, releasing Massachusetts and Western from the existing obligation and accepting in lieu thereof a mortgage on the Russell Ranch. Neither of the Bank's executives with whom this proposition was discussed knew anything about the Ranch or who owned it. They were at first 'extremely cool' towards the proposition because it meant making a new loan of additional money to the Massachusetts Group. Nevertheless, the Bank sent an appraiser to examine and report on the value of the property and finally told O'Flynn that it would advance Massachusetts the $20,000 requested and release the outstanding indebtedness of Massachusetts and Western, provided

> that the Bank's attorney, Thomas G. Greene, would approve the title and the validity of the Bank's proposed mortgage as a first lien on the property." (App. Br. 6-7)

There is no testimony in the record concerning the making of a *new loan.* On the contrary, Exhibit 29 (Tr. 379), a letter from the head office of the Bank to its branch, refers to the transaction as "a switch of liability". The testimony concerning knowledge of the Bank as to the ownership of the Ranch was that the Bank knew at the time of the transfer of the mortgage who owned the Ranch immediately prior to that time, or at least that Mr. Greene, its attorney, knew it and Mr. Greene's testimony was that the Bank knew what he knew. The Bank sent its appraiser to the property after it advanced to the Massachusetts at least a portion of the $20,000.00. Mr. Alward, Manager of the Portland Branch of the Bank, testified, "Yes, some money was advanced before we received our final report" (Tr. 364). All of the money was loaned before Mr. Greene made his report (Tr. 336, Ex. 27-a, b and c). The testimony is also to the effect that the Bank, prior to receiving transfer of the mortgage, loaned the Massachusetts $20,000.00 on the Massachusett's own note, secured by ample collateral, after investigating thoroughly its financial standing and after thoroughly investigating the collateral.

> (e) "Two years later the District Court rendered an opinion dated February 27, 1939, approving the order in part and disapproving it in part, and at the same time holding that appellant had acted in good faith in trying to collect its indebtedness and had paid valuable consideration for its mortgage." (App. Br. 11)

What the Court did was to sustain the Referee's Findings in full and approve the order made so far as restitution of the property was concerned. It set aside merely that portion which gave the Bank the option to pay the value of the property with interest from date of its acquisition (Tr. 111-2). The matter was re-referred solely for the purpose of determining whether under the allegations of Paragraph XIII of the Bank's Answer (Tr. 55-56) the Bank was entitled to offsets for improvements and advances made after it acquired the property. The Court held that the Bank acted in good faith merely in trying to *collect its indebtedness* and that the valuable consideration paid for the mortgage was merely the *cancellation of the debt owing to it by the Western.* See the Court's Opinion (Tr. 106-110, at p. 110), and see Judge Fee's Opinion on Rehearing (Tr. 188-213, at pp. 207-8) where it is said:

> "Unquestionably, as appears from the subsquent letter of O'Flynn and other evidence, Western intended to give and the Bank intended to get an unreasonable advantage over other creditors. This constitutes an intent to 'hinder, delay and defraud' other creditors, and a showing of actual fraud in the sense of gross and corrupt motive is not necessary to be shown. Under the language of Title 11, U.S.C.A. Sec. 110, Sub. a(4), if the creditor obtained undue advantage because of the transfer, it is fraudulent, although actual fraud be not shown, and the trustee is entitled to the property.
>
> "The finding of the Referee that the Bank did not purchase these lands in good faith must, in view of the authorities and the evidence, be affirmed. It was in good faith in trying to collect its indebtedness. It may be that every-

one involved believed no adjudication would be entered and that an upturn of values would make the bankrupt solvent, but in each instance events have decreed otherwise.

"The finding of fraudulent intent cuts into clear outline the positions with reference to money expended upon the property by the Bank." (See 44 Fed. Supp., Advance Sheets No. 1, pp. 89, 94, and Tr. 207-208.)

(3) Alleged Facts Based on Rejected Evidence

Many of the statements are based upon rejected testimony attempted to be brought into the case through affidavits accompanying the Bank's motion for a new trial. There is no specificaton of error charging that the Court erred in rejecting testimony nor does Appellant maintain that the decision should be reversed because of the erroneous rejection of testimony. Error cannot here be charged because the Court refused to give the Appellant's interpretation to the testimony offered as after-discovered evidence on motion for new trial, since the granting or denial of a motion for new trial based on after-discovered evidence is entirely in the discretion of the trial court and is not subject to review by an appellate court (see Discussion this Brief, pp. 30-31 post).

Now for specific examples:

(a) "Western pledged these two notes to Portland Trust Company, predecessor of Lawyers Title and Trust Company, trustee for the holders of Western's outstanding Series C installment bonds. These notes remained so pledged until new collateral was substituted and the mortgage discharged in February, 1932." (App. Br. 4)

These statements do not accurately state the facts, even based on the rejected evidence. The rejected evidence tended to show that the Western's mortgages to the Keystone were placed with a trust company, who thereafter resigned the trust, and that they were then deposited with another trust company and thereafter withdrawn. Had evidence not been rejected by the Referee, the Trustee would have shown, as to this phase, as he was in a position to show, that the latter trust company was also a mere alter ego of the Western controlled by O'Flynn, but, of course, there was no necessity for doing so under the circumstances. Moreover, the devastating fact shown by the Bank's own proffered evidence was that the mortgages claimed to have been substituted on Feb. 13, 1932, for the mortgages satisfied and withdrawn on that date were not executed until Feb. 27, two weeks after the satisfaction and withdrawal of the mortgages on the Ranch, nor were they recorded until May, 1932, three months later. (See Bank's proffered Exhibits 18 to 24 at the hearing before Referee Snedecor.)

> (b) "Ochoco thereupon issued its note for $55,960 to Massachusetts which note was secured by a mortgage on the Russell Ranch, in exchange for which Ochoco received certain assets, including mortgages on properties in Wahkiakum County, Washington, and Bend, Oregon, and these mortgages Ochoco transferred to Western in exchange for Western's satisfaction of the Keystone mortgage on the Russell Ranch. It was this Ochoco mortgage on the Russell Ranch which the Bank was to receive and ultimately did receive as security for its new loan to Massachusetts." (App. Br. 7-8)

As a matter of fact, the testimony showed that the Ochoco did not receive mortgages on properties in Wahkiakum County, Washington, and Bend, Oregon, from the Massachusetts in consideration of the $55,960.00 note and mortgage to the Massachusetts. The purported minutes of meeting of the Ochoco state that the mortgage was given because of the need by the Ochoco *to borrow money,* and the evidence showed that the Ochoco never did any business, never had a bank account and therefore never had any need for borrowing money (see Ex. 12, Tr. 291, 295). However, all of the Bank's statements above are based on the Appellant's interpretation of testimony *rejected.*

> (c) "Appellant put experts to work and found evidence establishing (a) that the Keystone mortgage had been paid prior to the filing of the bankruptcy petition, and (b) that the Keystone mortgage was not in the possession of the bankrupt when the petition in bankruptcy was filed, but was in the possession of the trustee of the bankrupt's bondholders." (App. Br. 12)

We assert, as Judge Fee asserted, that even the rejected evidence does not show that the Keystone mortgages had been paid (Tr. 200). However, this entire statement is based on Appellant's interpretation of the *rejected* evidence.

SYNOPSIS OF DISCUSSION FOLLOWING

I. Preliminary Legal Discussion

1. Findings of Fact made by a Referee, affirmed on review by the District Judge, must be treated as unassailable upon appeal, if there be any tes-

timony consistent with the finding.

2. The denial by the trial judge of a motion for a new trial based on newly discovered evidence will not be re-examined by the Appellate Court.

II. Questions of Jurisdiction

1. The Bankruptcy Court had summary jurisdiction to determine whether, after the filing of the petition in bankruptcy, the Bank had acquired property possessed by the Bankrupt at such time, and, if so determined, to require that such property be surrendered to the Trustee.
2. The Bankrupt at the time of the filing of the petition possessed the property in the Ranch, since the Keystone was not a claimant holding the Ranch adversely to the Bankrupt.
   (a) It was the agent of the Bankrupt
   (b) It was the alter ego of the Bankrupt (Piercing the Veil of Corporate Entity).
3. Keystone was not the holder of an adverse interest or of any interest in the mortgage.
4. Ownership of mortgage indebtedness is constructive possession of property, and if ownership in Bankrupt existed at bankruptcy, summary jurisdiction lies.
5. Possession of the mortgage (document) by Bankrupt was not essential when ownership of mortgage was actually in Bankrupt and stood in its name of record, with no assignment of ownership of record or otherwise to another.
6. Though the Bank may claim to be a bona fide purchaser for value of the Ranch, such claim,

assuming possession of the Ranch was in the Bankrupt at the time of bankruptcy, could not defeat the Bankruptcy Court's jurisdiction summarily to determine such claim.

7. Statements of the Bank that mortgage debt in favor of the Western had been paid, or had no value, or had been discharged by exchange of consideration, are not based on evidence before the Court. However, such questions are ones of fact, certainly not of jurisdiction, and since there was evidence to the contrary, this Court will not review the findings.
8. Drainage District Bonds transferred to Bank in same situation as transfer of Ranch.

III. Questions Concerning Improvements, Expenditures and Receipts

1. The Bank was not a bona fide purchaser for value.
2. Moneys paid after bankruptcy to another in order to obtain property of the Bankrupt cannot be recovered from the Bankrupt's estate.
3. The Bank, being in unlawful possession of the Ranch, will not be allowed credit for alleged permanent improvements, since it was not a purchaser in good faith without notice and for value.
4. The order concerning rental value of the Ranch merely fixed the value of the use of the Ranch, against which value allowed credits for advances may be offset; and although the determination be res adjudicata between the parties, it is not a judgment enforceable as such without further

court action.

5. Money paid to the Bank for a portion of land sold out of the land unlawfully acquired stands in lieu of the land itself, and the turnover order is proper, where money is still held.

I. PRELIMINARY LEGAL DISCUSSION

1. Finding of fact by a Referee, affirmed on review by the District Judge, must be treated as unassailable upon appeal, if there be any testimony consistent with the finding.

This doctrine was announced by the United States Supreme Court before the enactment of the present Bankruptcy Act, and therefore before the present General Orders in Bankruptcy were promulgated, and of course before the adoption of the Rules of Civil Procedure for the District Court of the United States. Rule of Civil Procedure No. 52(a) (made applicable to Bankruptcy matters by General Order No. 37) proclaimed this principle in the form of a Rule.

Said the United States Supreme Court in a decision written by Justice Brown, *Davis v. Schwartz* (1894) 155 U.S. 631, 637; 39 L. Ed. 289, 293:

> "As the case was referred by the court to a Master to report, not the evidence merely, but the facts of the case, and his conclusions of law thereon, we think that his finding, so far as it involves questions of fact, is attended by a presumption of correctness similar to that in the *case of a finding by a Referee,* the special verdict of a jury . . . or in an admiralty cause appealed to this court. In neither of these cases is

> the finding absolutely conclusive, as if there be no testimony tending to support it; but so far as it depends upon conflicting testimony or upon creditability of witnesses, *or so far as there is any testimony* consistent with the finding, it must be treated as unassailable."

Rule 52(a) of the Rules of Civil Procedure provides

> ". . . . Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the creditability of witnesses."

General Order in Bankruptcy No. 37, provides:

> "In proceedings under this Act, the Rules of Civil Procedure for the District Courts of the United States shall in so far as they are not inconsistent with the Act or with these general orders, be followed as near as may be."

Before the Federal Rules of Civil Procedure were promulgated or became effective (1938), this Circuit Court of Appeals also had occasion many times to apply the principle announced by the Supreme Court in Davis v. Schwartz (ante).

Said the late Judge Rudkin in *Hunter v. MacFarland* (1930) 45 Fed. (2d) 994:

> "The rule is too well settled to require citation of authority that such a report when approved by the trial court, is conclusive upon the appellate court, unless it appears that there was obvious error in the consideration of the facts, or a misapplication of some rule of law."

The late Judge Sawtelle stated on this Bench the same doctrine from another viewpoint, when he said in *In Re Duffy Players* (1931) 50 F. (2d) 737, 738:

> "The foregoing findings of fact by the Special Master and by the court below are based on substantial evidence, and are not to be disturbed by this tribunal."

And the same eminent jurist expressed again the same thoughts in the case of *Neece v. Durst* (1932), 61 F. (2d) 591, 593.

Judge Wilbur also expressed with brevity and positiveness the doctrine in *Wood v. Naimy* (1934), 69 F. (2d) 892, 895, and in *Swift v. Higgins* (1934), 72 F. (2d) 791, 796, when in the former case, he said:

> "We cannot disturb the findings of the Referee approved by the court, there being substantial evidence to support it."

Judge Garrecht gave like expression in the case of *Clements v. Choppin* (1934), 72 F. (2d) 766, 798, as did Judge St. Sure (sitting as an appellate judge) in *Hill v. Douglass* (1935), 78 F. (2d) 851, 853.

And after the promulgation of the Federal Rules of Civil Procedure, Judge Haney in the case of *Walker v. Lightfoot* (1941), 124 F. (2d) 3, 6, adverting to the *Rule 52 (a)* and *General Orders in Bankruptcy No.37,* said:

> "There was evidence supporting such findings and while there was some contrary evidence, we cannot say such findings were clearly erroneous."

The expressions of the Courts of Appeals of the other Circuits and of the Circuit Court of Appeals of the District of Columbia are in complete harmony.(1)

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(1) See Brannow v. Robbins (C.C.A.D.C.) 50 F. (2d) 499, 500. LeBlanc v. Fidelity Tr. Co. (C.C.A. 1st), 65 F. (2d) 442, 443. In Re Oriel (C.C.A. 2nd), 23 F. (2d) 409, 410.

Plack v. Banner (C.C.A. 3rd), 121 F. (2d) 676, 678.
Beneke v. Moss (C.C.A. 4th), 46 F. (2d) 948, 949.
Wetzel v. Schaefer (C.C.A. 5th), 124 F. (2d) 308, 310.
In Re Willoughby (C.C.A. 6th), 95 F. (2d) 932, 933.
Springmann v. Gary State Bank (C.C.A. 7th), 124 F. (2d) 678, 680.
Robbins v. Winters Creek Canal Co. (C.C.A. 8th), 109 F. (2d) 849, 851.
Alexander v. Theleman (C.C.A. 10th), 69 F. (2d) 610, 611.

We therefore conclude that the findings sustained and sustained again by the District Court will not be disturbed on appeal, since there was evidence on which to base such findings.

In order to lessen the labor of the Court and to show conclusively that there can be no review of the facts in this case, we shall in an appendix set forth seriatim all the findings of Referee Cannon upon the right of the Trustee to restitution and shall append after each some, though by no means all, of the evidence on which such finding was based.

As to the Findings of Referee Snedecor concerning alleged improvements, such findings were based solely on the uncontroverted testimony of a witness for the Bank, so there can be no question here as to the correctness of his findings adopted as they were by the trial court.

2. The denial by the Trial Judge of a Motion for New Trial, based on newly discovered evidence, will not be re-examined by the Appellate Court.

In *Pittsburgh, Cinn.-St. L. R. R. Co. v. Heck,* 12 Otto 120, 102 U.S. 102, 26 L. Ed. 58-59, Chief Justice Waite said:

> "We have uniformly held that as a motion for new trial in the courts of the United States is addressed to the discretion of the Court that

tried the cause, the action of that court in granting or refusing to grant such a motion cannot be assigned for error here."

See also the following:

Del. & H. R. Corp. v. Cottrell (C.C.A. 3rd) 69 Fed. (2d) 195, 198.
Shannon v. Shaffer Oil & Refining Co. (C.C. A. 10th) 51 Fed. (2d) 878, 881.
Erie R. Co. v. Irons (C.C.A. 3rd) 48 Fed. (2d) 60, 63.
N. Y. Life Ins. Co. v. Seifris, 46 Fed. (2d) 391, 393.
O'Brien v. General Acc. Fire & Life Assurance Corp., 42 Fed. (2d) 48-49.)
Henry v. Postal Telegraph Co., 100 Ore. 179, 187, 197 Pac. 258.

It is of interest to recall Judge Fee's statement in his opinion concerning the tendered "newly discovered" evidence. Said Judge Fee:

"The evidence tendered seems rather to strengthen than weaken the foundation." (Tr. 202)

It follows as a corollary of the law as thus expressed that evidence attempted to be presented as newly discovered evidence for the purpose of persuading the trial court to grant a new trial will not be reviewed by this Court to determine whether the Court exercised its discretion correctly, and certainly cannot be used for the purpose of determining whether the trial court should have originally reached a different conclusion than it did reach when such evidence was not before it.

II. QUESTIONS OF JURISDICTION

1. **The Bankruptcy Court had summary jurisdiction to determine whether, after the filing of the Petition in Bankruptcy, the Bank had acquired property possessed by the Bankrupt at such time, and, if so determined, to require that such property be surrendered to the Trustee.**

There need be no citation of authorities to maintain the proposition above. Both Referee Cannon and Judge Fee in their respective opinions cited numerous authorities to substantiate a like statement, and Appellant in its Brief (p. 23) now concedes such statement to be the law.

2. **The Bankrupt at the time of the filing of the Petition possessed property in the Ranch, since the Keystone was not a claimant holding the Ranch adversely to the Bankrupt.**

A. It Was the Agent of the Bankrupt

(Answering Appellant's Brief pp. 23-24)

The Appellant in its Brief urges that the Keystone held property in the Ranch adversely to the Bankrupt and that since the Bank traces its title through the Keystone, it therefore has the benefit of the adverse position of its predecessor in title. Disregarding for the moment the fact that the Western held a mortgage upon the Ranch for an amount in excess of its value, nevertheless the Bankruptcy Court had jurisdiction to determine the question whether or not one who holds property asserted to be the property of the Bankrupt holds such property adversely or whether it holds the same in the

interest of and as agent of the bankrupt. Of course, it is Hornbook Bankruptcy Law that where at the time of the filing of the petition, property of the Bankrupt is held by another, whom the trustee claimed holds in the interest of the Bankrupt as agent bailee or otherwise, the Court (Referee) has jurisdiction to examine into the claim of that person for the purpose of determining whether such claim is a pretense and therefore merely colorable or whether the claim of the so-called adverse party is really adverse. For the purpose of determining whether summary jurisdiction lies in the first instance, the petition of the Trustee is alone searched. It is for the Court, which includes the Referee, to determine this question. If it determines that the Trustee's petition sets up a case of ownership in the interest of the Bankrupt, it retains jurisdiction. If it finds that it does not, it relegates the parties to a plenary suit. Both Referee Cannon and Judge Fee examined this question with thoroughness. They concluded that the Keystone, under the allegations of the Trustee's petition, was the agent of the Western and was holding the title to the Ranch for the Western and that any claim to the contrary was merely a pretense. Then the Bank filed its Answer and denied, among other things, that Western possessed the Ranch at bankruptcy. It then became the obligation of the Trustee (again for the nonce disregarding the mortgage-ownership) to establish its position that the property was held by the Keystone in the interest of the Bankrupt, and that any adverse claim of interest in the Keystone

was a pretense and merely colorable. Certainly the Court had jurisdiction to determine this question upon the pleadings and the proof.

Said this Court in the late case of City of Long Beach v. Metcalf, 103 Fed. (2d) 483, 486:

> "Whether the bankruptcy court had jurisdiction of this proceeding must be determined by a consideration of the allegations of appellee's petition. Flanders v. Coleman, 250 U.S. 223, 227, 39 S. Ct. 472, 63 L. Ed. 948. Appellee's petition alleges that at the date of the filing of the petition in bankruptcy, the property in question was owned by, and was in possession of, the bankrupt. If so, the filing of the petition in bankruptcy brought the property into the custody of the bankruptcy court. Acme Harvester Co. v. Beckman Lumber Co., 222 U.S. 300, 307, 32 S. Ct. 96, 56 L. Ed. 208 (and other cases cited), and, upon adjudication, title to the property, with actual or constructive possession vested in appellee—the bankruptcy court's trustee—as of the date of the filing of the petition in bankruptcy. Mueller v. Nugent, 184 U.S. 1, 14, 22 S. Ct. 269, 46 L. Ed. 405 (and other cases cited).
>
> "Thereafter, notwithstanding Sec. 23, supra, the bankruptcy court, having possession of the property, had jurisdiction to hear and determine all questions respecting title thereto. Murphy v. John Hofman Co., 211 U.S. 562, 568, 29 S. Ct. 154, 53 L. Ed. 327 (and other cases cited). Whether such possession was actual or constructive is immaterial. Constructive possession was sufficient. Taubel-Scott-Kitzmiller Co. v. Fox, supra. We hold, therefore, that the bankruptcy court had jurisdiction of this proceeding. . . . . .
>
> "Appellants may, in their answer, deny any or all of the appellee's allegations, including the jurisdictional allegation that the bankrupt was in possession of the property at the date

of the filing of the petition in bankruptcy. Such denial, if made, will place on appellee the burden of proving the challenged allegations.

"If the jurisdictional allegation is proved by appellee or (hereafter) admitted by appellants, the referee should, and we assume that he will, then proceed to hear and determine the other issues raised by the petition and answer. If the jurisdictional allegation is not proved or admitted, the referee should, without considering any other issue, dismiss the proceeding."

This is an accurate and succinct statement of the law. The allegation of the Trustee's petition clearly stated that the Western was in possession and ownership of the Ranch but that the Keystone held said title "for and on behalf of the said Western Bond & Mortgage Co. as agent, subsidiary and alter ego of said Western Bond & Mortgage Co. and that before and after the filing of the petition in bankruptcy against the Western Bond & Mortgage Co. said Western Bond & Mortgage Co. in truth and in fact owned and was in possession of the fee of said Russell Ranch and owned and possessed said property" (Par. II of the Petition, Tr. 19, 21-22).

The Referee held that such allegation and others in the petition gave the Court summary jurisdiction to hear the matter (Tr. 38-45). The Bank in its petition denied these allegations and the burden was then upon the Trustee at the hearing to prove the same. He amply met this burden.

Upon the evidence adduced, the Referee and the Court concluded that the evidence sustained these allegations. This evidence was not only to the effect

that the Keystone was a wholly owned subsidiary of the Western, but it went much further than that. It showed that when the Keystone acquired title to the Russell Ranch, it obtained same from the Russell Land & Livestock Company (Ex. 15, Tr. 304), another wholly owned subsidiary of the Western (Ex. 7). There is no evidence in the record as to what it paid for the Ranch or that it paid anything for it. Immediately upon its acquisition and simultaneously (Tr. 304) therewith, it executed two notes aggregating $150,000.00 to the Western, its parent, and gave it a mortgage on the property to secure those notes (Ex. 16, Tr. 304-5). The evidence established that the Ranch property was never worth such sum (Tr. 386). All of the directors and officers of the Keystone were women employees of the Western —in fact were stenographers and clerks, having no executive authority or capacity and receiving no salary from the Keystone. They were in fact dummies to the full extent of that word used in corporate structures. They admittedly used no discretion as directors. They followed explicitly and without question the directions of the President of the Western. What he said, they did, without reasoning why and without objection or hesitancy. They responded to the slightest pull of the string by Western. The Keystone had no office of its own; its office was in the office of the Western. At the time of these transactions, it did no business whatsoever although formerly it had done, on behalf of the Western, a small loan business. The Western made a joint tax return to the federal government, including therein the

Keystone as one of its subsidiaries. No books of the Keystone were available, if any were ever kept; the Keystone made no adverse claim to the property. (For verification of these latter statements see pp. iv-viii Appendix, this Brief.) Therefore, as stated, the Referee and the Judge held that the Keystone was an instrumentality or agency of the Western in the possession of the ranch property. Certainly there was evidence in the record on which to base this finding, and as Judge Fee properly said, there was no necessity here, in order to find actual ownership or lack of adversity, for piercing the veil of corporate entity. The finding that the Keystone was the agent of the Western is amply supported.

B. It Was the Alter Ego of the Bankrupt (Piercing the Veil of Corporate Entity)

(Answering Appellant's Brief pp. 27-32)

However, if there be need to pierce the veil of corporate entity, the Court was certainly justified in piercing that veil in this instance, especially where it was found not merely that the Keystone was a wholly owned subsidiary of the Western but that it was its alter ego by virtue of the fact that it had no real corporate existence of its own except in form. Its whole activities were directed by puppets of the Western, holding merely qualifying shares in the Keystone. (In its Brief, the Bank repeatedly asserts that the entire ownership of the stock in a corporation will not justify piercing the veil of corporate entity—as though that was the only element present in this case. We agree that

that alone would not, without more, be sufficient. But there was more.)

In our Brief before the trial court we cited from a mass of authorities, twenty-one federal cases decided either by the United State Supreme Court or by the circuit courts wherein the veil was pierced. We shall not attempt to go through that process again. Many cases have been decided since that time to like effect. It will suffice to call to the Court's attention four cases only, three among the twenty-one cited in the court below, and one among the cases recently decided. We quote briefly from these four cases.

In *Chicago, M. & St. P. Ry. Co. v. Minneapolis Civic & Commerce Assn.*, 247 U.S. 490, 38 Sup. Ct. 553, 556-557, it is said:

> "The management and control of all the operations of the Eastern Company has always been kept in charge of a 'managing committee' of two members, one of whom for many years before the evidence was taken was the general manager of the Omaha Company and the other the general superintendent of the Milwaukee Company. The Eastern Company did not pay either of these men any salary for their services.
>
> "The auditor of the Omaha Company has been the auditor of the Eastern Company, which paid no part of his salary, and the established practice has long been for the one bookkeeper of the Eastern Company to take his journal and ledger to the auditor of the Omaha Company monthly for verification.
>
> "Seven of the nine directors of the Eastern Company at the time the evidence was taken were officers either of the Milwaukee or Omaha Company; the eighth, the attorney of the Eastern, had desk room in the Milwaukee Com-

pany's legal department, of which he had recently been a member; and the ninth director, the president, was not an employee of either of the two owning companies."

Upon these facts, the Court, through Mr. Justice Clarke, said:

"Much emphasis is laid upon statements made in various decisions of this court that ownership, alone, of capital stock in one corporation by another, does not create an identity of corporate interest between the two companies, or render the stockholding company the owner of the property of the other, or create the relation of principal and agent or representative between the two. . . . . .

"While the statements of the law thus relied upon are satisfactory in the connection in which they were used, they have been plainly and repeatedly held not applicable where stock ownership has been resorted to, not for the purpose of participating in the affairs of a corporation in the normal and usual manner, but for the purpose, as in this case, of controlling a subsidiary company so that it may be used as a mere agency for instrumentality of the owning company or companies. In such a case the courts will not permit themselves to be blinded or deceived by mere forms of law but, regardless of fictions, will deal with the substance of the transaction involved as if the corporate agency did not exist and as the justice of the case may require."

In the case of *Clere Clothing Co. v. Union T. & S. B. Co.* (C.C.A. 9th), 224 Fed. 363, Judge Morrow said:

"The Referee in Bankruptcy found as a fact that the Clere Clothing Co. and the Prager-Schlesinger Company were one and the same, the latter being merely an adjunct or instrumentality of the former; that to allow the Clothing Company's claims would be to permit it to

> prove debts against itself in fraud of creditors. The claims were accordingly disallowed and rejected. Upon review by the court below the order of the referee was affirmed. . . . . .
>
> "The fact that the two companies preserved separate entities does not detract in the slightest degree from the force of the facts adduced in the testimony hereinabove referred to."

And in *In re Eilers Husic House* (C.C.A. 9th), 270 Fed. 915 (Petition for certiorari denied, 42 Sup. Ct. 55), it was held that subsidiary corporations were so controlled by the dominant corporation, Eilers Music House, who owned most, though not all, of its stock, that the veil of corporate existence would be pierced and that the bankruptcy court would take summary jurisdiction of both concerns, notwithstanding the protest and contest of the subsidiary as an adverse claimant.

In *Stone v. Eacho* (C.C.A. 4th), 127 Fed. (2d) 284, 288-9, Judge Parker says:

> "It is well settled that courts will not be blinded by corporate forms nor permit them to be used to defeat public convenience, justify wrong or perpetrate fraud, but will look through the forms and behind the corporate entities involved to deal with the situation as justice may require (citing numerous cases) . . ."

and referring to the case of In Re Eilers Music House, he makes this comment:

> "In the case of In re Eilers Music House, supra, the assets of the subsidiary, which like the subsidiary here had no real separate existence, were ordered turned over to the trustee in bankruptcy of the parent in a summary proceeding upon a notice to show cause; and such a turnover order was approved in Fish v. East, 10 Cir. 114 Fed. (2d) 177, 191, and Tiller Bldg. Co. v. Reynolds (7th Cir.) 247 Fed. 90."

We also call to the attention of the Court the cases cited by Judge Fee in the notes to his opinion (Tr. 202-203).

Now the Appellant in its Brief (p. 24) maintains that if there exists a fair doubt and reasonable room for controversy as to the validity of the adverse claim, then the court has not summary jurisdiction, and cites three cases as authority for that statement. We deny the correctness of this position, and we deny that the decisions in the cases mentioned make such determination. But be that as it may, here in the case at bar there was no actual adverse holding by the Bank of the property prior to the filing of the petition in bankruptcy. As said in the case of *Adolph Ramish, Inc. v. Laugharn* (C.C.A. 9th), 86 Fed. (2d) 686-688, one of the cases cited by Appellant,

> "The transfer to Appellant came after the petition."

So, too, did it come in the case at bar. Hence no claim of adverse holding can be made by the Bank in its own right. It must, and does now, claim (although such claim was not made below) that it traces its right through the alleged adverse ownership of the Keystone.

But there was no claim of such adverse holding, *by Keystone.* Its President, Miss E. E. Gallagher, was one of the witnesses at the hearing—the only officer of the Keystone, or for that matter of any of the controlled or controlling corporations, to testify. She testified that she, Miss Thibodeaux, Miss Smith and Miss O'Reilly were all the officers and directors

of the Keystone and that there were no other employees of the Keystone (Tr. 303); that they were all office employees of the Western (Tr. 282, 283, 294, 297, 303); that she and Miss Thibodeaux were directors of the Western (Tr. 271, 281); that none of them received any compensation from Keystone; and that none of them had any interest in the Keystone except as a holder of one qualifying share each for which someone else, she did not know who, paid (Tr. 299). She and the other officers and directors of the Keystone acted only to carry out the desires of the president of the Western (Tr. 295). Though president of the Keystone, she could not say or remember whether it did any business whatsoever at or about the time of the transfer of this Ranch, or at any time in 1932. She did not know whether the Keystone was then dissolved. She made no claim or statement that it was holding the property in its own right. Where, then, comes the belated claim by the Bank that its claim of adverseness comes through the adverse position of the Keystone? Certainly there was no evidence presented to show that the Keystone was holding adversely, and all the evidence was to the contrary.

In Appellant's Brief on pages 26 and 27, it stresses its position that any contested matter is an adverse matter, saying

> "Appellee will deny that the Keystone's title was adverse. This very denial, however, entitled the Bank to a plenary trial before a court or jury since the issue, upon the facts already stated, indisputably constitutes 'a contested matter of right involving some fair doubt and reasonable room for controversy'" (p. 27).

This argument is, indeed, fallacious for if it is taken to be true, no summary proceedings could ever be maintained where the party against whom it is sought claimed that he has an adverse interest. One may be sure that such a claim would always be made. Thus, summary proceedings could only be brought by consent, which, of course, is not the law. Appellant cites in this connection six cases. We call attention to the fact that in all these cases, the claim which was asserted by the litigant to be adverse was a claim which the *litigant* had acquired *prior* to the filing of the petition in bankruptcy. In this case, possession by the Bank was acquired after the filing of the petition. We tabulate these cases, with data showing that the litigant's possession in every case arose prior to bankruptcy.

Name of Case	Date Possession Taken or Lien Acquired	Date of Filing Petition
In re Club New Yorker, 14 Fed. Sup. 694	Dec. 31, 1935	Jan. 10, 1936
Buss v. Long Island Storage Co., 64 Fed. (2d) 338	Dec. 5, 1930	Approx. 6 mos. thereafter
Mueller v. Nugent, 184 U.S. 15, 46 L. Ed. 411	Feb. 9, 1900	Feb. 19, 1900
Harrison v. Chamberlain, 271 U. S. 191 (1)	Aug. 30, 1917	May 25, 1921
Shea v. Lewis, 206 Fed. 877	Prior to Filing Petition (see Opinion p. 82)	August 9, 1911
Marcell v. Engebretson, 74 Fed. (2d) 93	Feb. 16, 1942	August 9, 1929

Before closing this portion of the Brief, we call to the Court's attention the erroneous statement made on page 27 of Appellant's Brief that, "The

(1) In all the above cases except this one the dates were obtained from the opinion itself, or from the opinion below, but in this instance the source of the dates is the Transcript of Record in that case pp. 1 and 14.

lower court made no finding that Keystone's claim was colorable." We call attention to Findings (3) and (4), (Tr. 71). If these are not findings of fact determining that the Keystone's holding was merely colorable, it would be hard to frame such a finding, except to state in the language of a conclusion that such holding was colorable.

3. Keystone was not the holder of an adverse interest or of any interest in the mortgage.

Nevertheless, even if it be considered that the holding of the fee title to the property by the Keystone was adverse to the Western, which we confidently assert we have shown it was not, and if it be further considered that Appellant's position on that phase is correct, which of course we protest it is not, still there can be no question that the Western at the time of the filing of the petition in bankruptcy held a claim against the Keystone secured by a transfer of property by means of the mortgage to the Western, and that therefore, the Keystone held no adverse or other interest whatsoever in the secured indebtedness *owing by it* to the Western or in the security which it had transferred to the Western by means of the mortgage, and this, irrespective of the fact that the mortgage secured notes in the amount of $150,000.00, far in excess of the value of the Ranch, found to be of a value of $65,000.00. So it can be safely premised that the Keystone held no interest adverse to the Western in the mortgage against the property, nor in the debt secured by the mortgage.

4. Ownership of mortgage-indebtedness is constructive possession of property, and if ownership in Bankrupt existed at bankruptcy, summary jurisdiction lies.

(Answering Appellant's Brief pp. 37-41)

Under a preceding heading, we have discussed the question of ownership of the Ranch itself at the time of bankruptcy. Appellant argues that ownership of the mortgage is not ownership of the Ranch property and that in order to recover the Ranch property it is not sufficient to establish the fact that the bankrupt held a mortgage thereon. The position of the Trustee is that ownership of the mortgage indebtedness in the Bankrupt at the time of bankruptcy draws to the Court summary jurisdiction to determine questions concerning that indebtedness and concerning the property held as security therefor to the extent, at least, of the security. It is unquestioned that after bankruptcy the bankrupt destroyed that security and obliterated the indebtedness by satisfying the mortgage and indebtedness of record. It was through the satisfaction of the mortgage which, as stated, was in a value at least equal to the value of the property, that the Bank was enabled to obtain its mortgage upon the Ranch property. Had not the Bankrupt satisfied that mortgage, recorded in its name, the Bank could not have obtained a first lien upon the property through the devious conveyances, mortgages and assignments heretofore referred to. Thus, at the time the Trustee qualified, he would have held, in the interest of

the bankrupt estate, a mortgage against the Russell Ranch securing an indebtedness of $150,000.00, which he, instead of the Bank, could have foreclosed. It was the acquisition by the Bank of the mortgage, through the recording of the various papers held in escrow with its attorney, including that of the satisfaction, that gave the Bank title through foreclosure. The Bank, therefore, can be required to return that property in a summary proceedings, to the Trustee for the benefit of the creditors. There would be no essential difference in principle if, instead of the devious methods employed, the Bank had taken an assignment directly from the Western of the Keystone's mortgage and notes. Had such been done after bankruptcy, could it be questioned that the bankruptcy court would have had summary jurisdiction to require the Bank to cancel such mortgage, or had the Bank foreclosed thereon, to return the property which it had obtained through such foreclosure?

Aptly did Judge Fee, quoting from *May v. Henderson,* 268 U.S. 111, say in this connection in his opinion (Tr. 205):

> "The Bank, which obtained this asset by whatever devious process, should be required to return it. 'Any other rule would leave the Bankruptcy Court powerless to deal in an effective way with those holding property for the bankrupt, who, pending the bankruptcy proceedings, wilfully dispose of it by placing it beyond the reach of the court.' May v. Henderson, supra, 118."

It has been often determined by various courts throughout the federal judicial system that notes,

bonds, accounts, stocks, rights to seats on stock exchanges, and other choses in action owned by the Bankrupt at the time of filing the petition are in its constructive possession and are brought into the jurisdiction of the bankruptcy court.

From the mass of such authorities we choose quotations from seven, among them one from the Supreme Court and two from this Circuit.

In *Acme Harvester Co. v. Beekman Lumber Co.*, 222 U.S. 300, 22 Sup. Ct. 96, 99, 56 L. Ed. 208, Justice Day said:

> "There is no dispute upon the record that the money attached *was owing to the bankrupt*, and was unquestionably its property. . . . The exclusive jurisdiction of the bankruptcy court is so far in rem that the estate is regarded as in custodia legis from the filing of the petition."

In *In Re Ransford* (C.C.A. 6th), 194 Fed. 658, 663, the Court says:

> "The title to the indebtedness of the bank was in the trustee (Acme Harvester Co. v. Beekman Lumber Co., 222 U.S. 300, 32 Sup. Ct. 96, 56 L. Ed. 208), and we think for the purposes of this suit should be regarded as constructively in his possession, and that the District Court had jurisdiction to proceed summarily to determine the rights of the parties."

In *In re Orinoco Iron Co. v. Metzel* (C.C.A. 6th), 230 Fed. 40, 44-45, it is said:

> "Was the fund in question in the custody of the bankruptcy court? The rule which gives the bankruptcy court exclusive jurisdiction to determine claims to property in its custody is not limited to actual possession, but extends to constructive possession as well, including

property held not only by but for the bankrupt (citing numerous cases). And we have held that a debt due the bankrupt's estate is so far constructively in the trustee's possession as to give the bankruptcy court jurisdiction to determine the rights of parties to it. In re Ransford, 194 Fed. 658, 664, 115 C.C.A. 550."

In *In re Worrall* (C.C.A. 2nd), 79 Fed. (2d) 88, 89, it is said:

> "The decisions are numerous that, if the bankrupt remained the legal owner of the chose in action up to the time of the filing of the petition . . . . his control was such that a trustee in bankruptcy who succeeded him was to be regarded as in 'possession' of the chose in action and as in a position summarily to determine his rights as against other claimants."

And in *In re Borok* (C.C.A. 2nd), 50 Fed. (2d) 75, 79, it is said:

> "One cannot speak of 'possession' of a chose in action in the same sense as of tangibles, but if such terminology is to be used, it would seem that the bankrupt was as much in possession of the assigned accounts as he could be of any chose in action."

Said Judge Wilbur in *Seattle Curb Exchange v. Knight* (C.C.A. 9th), 46 Fed. (2d) 34, 35:

> "The question involved on this appeal is whether or not the right to the proceeds of the sale of the seat in the Seattle Curb Exchange, as between the trustee in bankruptcy and the Seattle Curb Exchange, must be litigated in the bankruptcy court to the exclusion of the state court. This turns upon the primary question as to whether or not the seat came into the custody of the bankruptcy court at the time of the filing of the petition of bankruptcy or of the adjudication of bankruptcy. That question was carefully and exhaustively considered by Judge

Lurton, then of the Circuit Court of Appeals of the Sixth Circuit, in O'Dell v. Boyden, 150 Fed. 731, 736, 10 Ann. Cas. 239. In that case it was said:

> " 'The "seat" or "membership" continued to be the "seat" of Henrotin (one of the bankrupt partners), and was a pecuniary asset which passed to his trustee. It was as much in his custody and possession as such a species of property is capable of. To deny the trustee's possession would be to deny the capability of possession of a chose in action or other incorporeal right or equity. The possession may be constructive, and not manual; but it is only so because such property is not capable of a more tangible custody.' "

In *Street v. Pacific Indemnity Co.* (C.C.A. 9th, 61 Fed. (2d) 106, 107-109, Judge Sawtelle said:

> "The appellant contends that at the time of filing the petition in bankruptcy the money here sought to be recovered by the trustee was in the possession of the county of Alameda, being held for the account of the bankrupt, and therefore in the constructive possession of the bankruptcy court and subject to the summary jurisdiction thereof. It is his contention that the money was paid by the county to appellee pursuant to the assignment . . . nine days after the filing of the petition in bankruptcy, at which time the money was already in custodia legis, and therefore could not be affected by said assignment.
>
> "The authorities are clear that the summary jurisdiction of the bankruptcy court attaches at the time the petition in bankruptcy is filed (citing numerous cases). It therefore becomes necessary to determine the status of the money herein involved at that time. . . .
>
> . . . . . .
>
> "The $6,327.07 . . . held by the county . . . at the time the petition was filed, came within

> the constructive possession of the bankruptcy court and subject to its summary jurisdiction. If it were possible to take away that summary jurisdiction by merely turning the property over to one who has a claim against it, the administration of bankrupts' estates would be greatly retarded and unduly hampered."

We assert, therefore, that whether or not the Bankrupt at the time of bankruptcy had possession or ownership of the Ranch property itself through its agent or alter ego, the Keystone, it certainly had possession of the indebtedness against the Ranch secured by the mortgage, and having possession thereof, the Court had summary jurisdiction to place the Bankrupt, as nearly as practical, in the same status as it was at the time of bankruptcy.

5. Possession of the mortgage (document) by Bankrupt was not essential when ownership of mortgage was actually in Bankrupt and stood in its name of record, with no assignment of ownership of record or otherwise to another.

(Answering Appellant's Brief p. 42)

Appellant in its Brief says that in 1931 the mortgage had been pledged by the Bankrupt to the Portland Trust Company as security under a trust indenture to secure outstanding bonds of the Bankrupt and that it so remained until the transaction complained of. There is no evidence in the record on which to base a statement, except the Bank's interpretation of the rejected evidence. Had not this evidence been properly rejected, the Trustee, as heretofore stated, would have introduced evidence showing that this Company did not hold such mort-

gage document but that it was supposedly held by a company called the Lawyers Title and Trust Co., an organization entirely owned and controlled in the interest of the Bankrupt, that there was no trust indenture of record and that the so-called bonds which were claimed to have been secured by this fictitious deposit of the document were merely certificates of indebtedness held by creditors, most of whom had filed their claims in the bankruptcy proceedings. But such course was not necessary.

Be all that as it may, however, the controlling devastating fact remains that the Western had sufficient possession of the mortgage to satisfy the same of record and to satisfy the obligation which it secured. Possesison in a bankrupt at or after bankruptcy sufficient to surrender property is certainly sufficeint to give the court jurisdiction over the property surrendered after bankruptcy.

Moreover, it is provided under the Oregon statutes, as follows:

Section 70-127, O.C.L.A.:

> "Separate books shall be provided by the County Clerk in each county for the recording of deeds and mortgages."

Section 70-130, O.C.L.A.:

> "Every conveyance affecting the title of real property within this state hereafter made which shall not be recorded as provided in this title shall be void as against subsequent purchasers in good faith and for a valuable consideration. . . . ."

Since the Trustee in bankruptcy, under the Bankruptcy Act, is in the position of a bona fide pur-

chaser for value, the mere possession of a mortgage document by another is ineffective and void as against a Trustee in bankruptcy.

If the rejected evidence be considered, which we insist it cannot be, still the facts in the case of *In re Bastanchury Corp.*, 62 Fed. (2d) 537, 542, cited by Appellant at p. 42 of its Brief, are of an entirely different nature. There, after default, a Trustee under a trust indenture took possession of the property in the interest of the beneficiares of the trust on January 25, 1932, and at the time of bankruptcy, March 21, 1932, was holding and operating said property (see page 538 of the decision). The Trustee in that case claimed that the Bastanchury Corp. was holding as agent of the Bankrupt, since under California law a Trustee in a trust indenture is agent for both the Trustee and the beneficiary. But the Court held that such position was subject to qualification, that is to say, that until default he might so hold, but that after default, he holds in the interest of the beneficiaries, at least until the indebtedness to the beneficiaries is satisfied. There default had occurred. It was in this connection that the Bank said that a real controversy in law existed and that there was at the least a "fair doubt and reasonable room for controversy as to the validity of the adverse claim." So we see merely that where *prior* to bankruptcy possession was taken by the litigant under a right which the Court held was probably sustainable, that the matter should be relegated to a plenary suit.

6. Though the Bank may claim to be a bona fide purchaser for value of the Ranch, such claim, assuming possession was in the Bankrupt at the time of bankruptcy, could not defeat the Court's jurisdiction summarily to determine such claim.

(Answering Appellant's Brief pp. 32-37)

So startling is the Appellant's assertion that the mere claim that it was a bona fide purchaser of the property after bankruptcy defeats summary jurisdiction, that we have read and reread this portion of the Brief to discover if we may not have misinterpreted the Appellant's position.

There is no such law. Given the fact that the Bankrupt had possession of the property at the time of bankruptcy, the claim that the litigant was a bona fide purchaser after bankruptcy is determinable in a summary proceeding. Of course, if the bankrupt did not have possession of the property in question at the time of bankruptcy, then the litigant was or was not a bona fide purchaser, no such summary jurisdiction would exist. If the mere claim that one is a bona fide purchaser would defeat jurisdiction over property owned by the Bankrupt at the time of bankruptcy, then Bankruptcy Courts would be impotent to administer bankrupts' estates and would be at the mercy of anyone who could grab the bankrupt's property before a Trustee was appointed, claiming thereafter to be a bona fide purchaser of it. Thus would the Trustee be forced into plenary suits to bring back to the Bankruptcy Court property which it had in its jurisdiction upon the filing of the petition.

Obviously, the Bank has little confidence in its

assertions that the mere *claim* of bona fides is sufficient to defeat summary jurisdiction since it indulges in three pages of argument (pp. 35-37) in the endeavor to show that it established in the court below that it actually was a bona fide purchaser. The Bankruptcy Court three times (two Referees and the Judge) found, after examining the evidence, it was not. If the mere claim of bona fides were sufficient to defeat jurisdiction, the matter ends; if not, then the determination made by the Referees and the Judge will not here be reviewed, since such finding was made upon substantial evidence. (We shall discuss the factual question of bona fides in a later portion of this Brief, pp. 63 to 72.)

The Appellant discusses at pp. 33-34 of its Brief, the case of Morrison v. Bay Parkway National Bank (C.C.A. 2nd), 60 Fed. (2d) 41, and cites six other cases (at p. 34) claimed to be of like effect in substantiation of the proposition that where a litigant claims to be bona fide purchaser of the Bankrupt's property after bankruptcy from one other than the Bankrupt, summary jurisdiction will not lie. The cases do not so hold.

In the *Morrison v. Bay Parkway National Bank* case, supra, one Zalta was adjudicated bankrupt on July 21, 1930. The Trustee, Morrison, brought suit against the Bay Parkway National Bank to set aside a preference given within four months prior to the filing of the petition in bankruptcy and recovered a judgment against the Parkway Bank for the recovery of that preference. Sometime after the adjudication in bankruptcy, the Lafayette National

Bank purchased the Parkway Bank, and assumed to pay all the debts of the Parkway Bank. The Lafayette Bank had no notice of the Trustee's claim or its suit against the Parkway Bank. The Trustee sought, in a summary proceedings, to recover *from the Lafayette Bank* the preference which the bankrupt, Zalta, four months prior to the filing of the petition in bankruptcy had by payment given *to the Parkway Bank.* The Trustee maintained, first, that in view of the fact that the Lafayette Bank had assumed to pay all the indebtedness of the Parkway Bank, the adjudicated preference given by the bankrupt Zalta to the Parkway Bank was assumed. The Trustee further maintained that he, having obtained judgment for recovery of this preference given by Zalta to the Parkway Bank, and the Lafayette Bank, having received the assets of the Parkway Bank, it could follow those assets in the hands of the Lafayette Bank. The court held that a Trustee could not recover in a summary proceedings upon a breach of contract, even if the contract had been assumed by the transferee of a preferred creditor who had received the preference prior to bankruptcy, nor could the Trustee recover even if the specific funds of the Parkway Bank were traceable in the hands of the Lafayette Bank, particularly where the Lafayette Bank was a bona fide purchaser of the assets of the Parkway Bank without notice of any claim on the part of the Trustee. (The Parkway Bank was not the bankrupt.)

From these facts it will be seen that whatever claim the Trustee in bankruptcy had against the Lafayette Bank, he had by reason of a transfer or preferential payment which had occurred within four months prior to the filing of the petition. Under such circumstances, it is not maintained, and could not be maintained, that a summary suit would lie for the recovery thereof. As the Court very aptly said

> "Zalta is not shown to have had any property in the hands of either Bay Parkway Bank or the Lafayette Bank at the time the petition in bankruptcy was filed."

The quotation made from that case, therefore, on pages 33 and 34 of the Appellant's Brief must be taken and read in the light of the facts.

The case of *Myers v. Hazzard* (C.C. Neb.), 50 Fed. 155 is not a decision concerning summary jurisdiction or jurisdiction at all. The facts in this case are as follows:

George Hazzard, the bankrupt, was at the time of his bankruptcy the owner of an interest in cattle held in the name of Foster & Struthers, and which Foster & Struthers had mortgaged to John Hazzard to secure a number of negotiable notes with the understanding that he would negotiate the notes, and out of their proceeds, pay certain prior encumbrances. He sold the notes to one Coates who was a bona fide purchaser of said notes before maturity and without notice, and the court merely held that the bona fide purchaser of a negotiable note prior to maturity acquired rights under a mortgage which was given to secure that note superior to those of

a Trustee in bankruptcy of the beneficial owner of the chatels mortgaged. The court determined from the facts presented that Coates was a purchaser in good faith, for present consideration, of the notes in question and that having no actual knowledge of the filing of the petition in bankruptcy against Hazzard, that he was also a purchaser without notice. The Court in this case also held that:

> "At the time of the assignment of the notes and mortgage to Coates, the mortgaged property was not in custodia legis." (p. 163)

(We also call attention to the Court that this decision under the Bankruptcy Act of 1867 which did not give the summary jurisdiction to the Bankruptcy Court given under the present act.)

And so in *In re Mullen* (D.C. Mass.), 101 Fed. 413, the facts are that in 1892 Mullen transferred to his wife certain property. Six years thereafter the wife died, and one year after that Mullen filed a petition in bankruptcy. Two days after the filing of the petition, and in fact after the adjudication, for the petition was a voluntary one, the Continental National Bank to which Mrs. Mullen owed money, sued her Administrator and attached the real property in question and thereafter judgment was obtained and the property levied upon. The Trustee in bankruptcy brought summary proceedings against the Continental Bank to require it to reconvey the property to the bankrupt estate. Upon objections filed in the summary proceedings, the Referee overruled such objections and when the matter came up for review before the court, the court disapproved of the method of thus deter-

mining the case, indicating that the Referee should have also found upon the merits, and said:

> "As, however, all parties are desirous that the questions of law should now be settled and as *it lies in my discretion* to pass upon them at this time, I shall not send the case back to the Referee for further hearing."

From this remark it is obvious the court had determined that summary proceedings would lie, or otherwise it could not send the case back to the Referee for further hearing. The case was heard upon its merits by the court in a summary proceedings. The court merely held that since the conveyance to the wife had been made more than four months prior to the filing of the petition in bankruptcy, the right of an attaching creditor against the property was superior to that of a Trustee in bankruptcy. At that time, the Trustee's rights were those *only* of the bankrupt's creditors, which, under the law of Massachusetts, were inferior to the rights of a prior attaching creditor of the fraudulent grantee, who had no notice of the fraud or of the bankruptcy proceedings. However, it may be said in passing that had this suit been brought after the amendment of 1912 to Sec. 47(a), the Trustee would have prevailed, because under that amendment the Trustee is vested with all rights, remedies and powers of a judgment creditor holding an execution duly returned unsatisfied. So, the decision in that case is merely and only to the effect that under the law as it stood in 1900 the attaching creditor of a fraudulent grantee had superior rights under Section 70(e) to those of a Trustee in bankruptcy, which the

amendment of 1910 attempted to remedy.

The case of *Paddock v. Fish* (D.C.S.D.N.Y.), 10 Fed. 125, also arising under the Bankruptcy Act of 1867, is not a decision in any manner upon jurisdiction, summary or otherwise, and it merely determines the right of a trustee in bankruptcy under the restricted Act of 1867 where property is alleged to have been fraudulently conveyed prior to bankruptcy.

The case of *Bennett v. Semmes* (D.C.E.D. Ark.), 287 Fed. 745, is a plenary suit brought by the Trustee in bankruptcy to set aside a trust deed given within four months *prior* to bankruptcy to secure notes of the bankrupt. There is no question in the case of jurisdiction, summary of plenary. The case is one which was essentially determined by the Uniform Negotiable Instrument Law.

Neither the case of Gray v. Breslof, 273 Fed. 526, nor the case of Peninsular Bank v. Wolcott, 232 Fed. 68, involves the question of jurisdiction and both were cases brought to set aside preferential transfers given within four months prior to bankruptcy.

We assert, therefore, with positiveness that the claim that one is a bona fide purchaser for value of the Bankrupt's property acquired after bankruptcy is a matter to be properly determined in a summary proceedings upon the facts presented. As heretofore stated, the facts were presented in the summary proceedings and the Referees and the Judge all held that the Bank was not a bona fide purchaser. This should end the matter so far as

that phase of the case is concerned, since there was substantial evidence below on which to base such finding.

7. **Statements of the Bank that mortgage debt in favor of the Western had been paid or had no value, or had been discharged by exchange of consideration, are not based on evidence before the Court. However, such questions are ones of fact, certainly not of jurisdiction, and since there was evidence to the contrary, this Court will not review the findings.**

(Answering Appellant's Brief pp. 42-47)

The Appellant in its Brief under heading "C-3, 4 and 5) bases its statements and arguments almost entirely upon rejected evidence. The flimsy post mortem attempt to show that the mortgage had been paid resulted in the rejection by Referee Snedecor of the proffered evidence. Again, where such evidence was submitted through affidavits upon motion for rehearing, Judge Fee, though holding that the Bank was precluded by laches from petitioning for a rehearing, did consider the so-called newly discovered evidence, part of which concerned that of the alleged payment. Said the Judge in this connection:

> "The newly discovered evidence, which it is claimed indicates that the mortgages were paid in full by Western, is unsatisfactory. Even if the money went into the account of a subsidiary, it is clear Western had full control of such accounts and withdrew from them at its pleasure. Besides, there is no showing that these amounts were paid in satisfaction of the mort-

gages. Western left the mortgages in the trust account after it is claimed they were paid." (Tr. 200)

But we insist that such evidence, however flimsy, is not in this case, since it was presented on motion for a rehearing which motion was denied. (See pp. 30-31 ante, this Brief.)

The same remarks are applicable to the claim by the Bank that if the mortgage existed at all and had value, it was exchanged for consideration of equal value. Evidence was attempted to be introduced that the Western had received after bankruptcy other mortgages in consideration for the mortgage which it satisfied in order to give the Bank title. This so-called newly discovered evidence was likewise rejected by Referee Snedecor, and such evidence when presented upon motion for new trial was held by Judge Fee of no weight. (See Trustee's Ex. 18-C (Tr. 593.) Moreover, as to the preposterousness of the claim of the Bank, we recall to the Court's attention that the satisfaction by the Western of the mortgage upon the Russell Ranch was executed the 13th day of February, 1932, and on that day placed in escrow with the Bank's attorney (see Trustee's Ex. 17, Tr. 305, and Trustee's Ex. 24, Tr. 314-315). The Bank's tendered exhibits 18 and 23 are two mortgages in the forms of deeds securing notes of $225,000.00 executed by the Realty Securities Co. to the Ochoco Farms Corporation upon real property in Wahkiakum County, Washington, and Bend, Oregon. They are signed in the name of the Realty Securities Co. by E. E. Gal-

lagher, President, and B. O'Reilly, Secretary, of whom much has heretofore been said. Both of these mortgages are dated February 27, 1932, and show recordation on May 12, 1932. The Bank's tendered exhibits 22 and 24 show an assignment of these mortgages to the Western by Ochoco, dated likewise on February 27, 1932 and show recordation on May 12, 1932. They, too, are signed in the name of the Ochoco by E. E. Gallagher, President, and B. O'Reilly, Secretary. It will therefore be noted that the satisfaction of the mortgage which the Bank claims was traded for the assigned mortgages of the Realty Securities Co. antedated by two weeks the execution of such assigned mortgages, and by three months their recordation. In other words, it is obvious when the Western satisfied its mortgage upon the Russel Ranch, the mortgages which the Bank claims were traded for such satisfaction were not even in existence. This, to say nothing of the fact that the pleadings and order in the same bankruptcy matter against another claimant tendered by the Trustee (Ex. 18-C, Tr. 593) showed that the property on which the Realty Securities Company's mortgages were given were in the process of foreclosure for taxes far in excess of any value of the property, and that the Court found in that matter that the mortgages of the Realty Securities Co. had no value. We recite these facts not because they have any bearing in this matter but to show the deceptive character of the so-called newly discovered evidence. In disregarding the proferred evidence, well did Judge Fee remark that "The fictitious nature of the

entire transaction is obvious."

Be all this as it may, however, we again revert to the statement that this proffered evidence was rejected by the Referee and that a new trial based thereon was denied by the Court. It therefore cannot properly be considered by this Court in this case.

Under Appellant's heading "C-5", it is stated that "We have presented the issues on the assumption that the [rejected] evidence is properly before the Court". Our only comment upon this is that undoubtedly the assumption is entirely erroneous. We again refer to the discussion in this Brief, pp. 30-31 ante.

8. Drainage District Bonds transferred to Bank in same situation as transfer of Ranch.

We will not take valuable space in this Brief to discuss this phase. We assert that the bonds, after bankruptcy, were in the possession of the bankrupt, and that, through the fictitious Ochoco, were transferred to the Bank. It is in the situation of the Ranch, except here there is no question of agency or alter ego of Keystone.

III. QUESTIONS CONCERNING IMPROVEMENTS, EXPENDITURES AND RECEIPTS

1. The Bank was not a bona fide purchaser for value.

We now approach that phase of the matter involving Referee Snedecor's findings and Judge Fee's adoption thereof.

No question of jurisdiction is here involved. The consideration of the question of the allowance of a credit to the Bank for expenditures for improvements, taxes, rental of grazing lands and even of the payment of moneys to the Massachusetts—if the latter is here involved at all—depends upon a determination of whether or not this Court will review the findings of Referee Cannon and of Referee Snedecor, both approved by the Judge, to the effect that the Bank was a purchaser in good faith, without notice, and for valuable consideration, that is to say, a bona fide purchaser. We therefore discuss this question first.

Referee Cannon found in this regard:

> "That . . . . the Western Bond & Mortgage Company, without receiving any consideration therefor released and satisfied the said mortgages which it held against said property." (Finding 9, Tr. 74.)
>
> See also Finding 13, Tr. 76-77.
>
> "That no present consideration, fair or otherwise, was paid by the Bank of California, National Association, for the said Russell Ranch or for the said Drainage District Bonds." (Finding 20, Tr. 79.)
>
> "That the Bank of California, National Association, had actual knowledge . . . of the filing of the petition in bankruptcy against the Western Bond & Mortgage Company and had actual knowledge . . . of the ownership by the Western Bond & Mortgage Company of the . . . mortgages upon said Russell Ranch to secure the payment of said notes and of the recordation thereof . . . and that the recordation of the satisfaction of the mortgages . . . would deprive the Western Bond & Mortgage Company of its property rights in said Ranch." (Finding

16, Tr. 77-78)

"That the estate in bankruptcy of the Western Bond & Mortgage Company was diminished to the extent of the value of said Russell Ranch and of the value of said Bonds and that said diminution occurred after the filing of the petition in bankruptcy to the knowledge of the Bank of California, National Association." (Finding 19, Tr. 79.) See also Finding 17, Tr. 78-79.

"That said transactions . . . was . . . out of the ordinary course of business of said Western Bond & Mortgage Company and of said Bank of California, National Association." (Finding 21, Tr. 79)

"That the acquisition of said property . . . . by the Bank of California, National Association, was a fraud upon the creditors of the Western Bond & Mortgage Company and a fraud upon the bankruptcy estate of said Western Bond & Mortgage Company." (Conclusion of Law No. (3), Tr. 80)

Referee Snedecor found:

"The Bank was not an innocent purchaser of the Ranch for valuable consideration and without notice of any infirmity in the title it acquired." (Finding 13, Tr. 134)

"The Bank knew that the grantor's capacity to execute a valid conveyance was in litigation. The Bank, in an attempt to obtain an advantage over other creditors, acted before that litigation was concluded. The Bank knowingly took the obvious chance that the conveyance might be defeated by the subsequent adjudication of the grantor, and with this knowledge, proceeded to treat the property as its own. In the opinion of the referee this is not the 'good faith' which should impel a court of equity to protect the Bank." (Finding 17, Tr. 137)

"The Bank of California, N.A., did not purchase the Russell Ranch in good faith and therefore it should not be permitted to recover the

value of any improvements made by it." (Finding 19, Tr. 139)

Judge Fee approved Referee Cannon's Findings and confirmed those of Referee Snedecor. In his opinion in the case, among other things, Judge Fee said:

> "The Bankrupt received no present consideration for the removal of this asset." (Tr. 205)
>
> "It must be kept in mind that all the dealings of the Bank with this property took place after the filing of the petition *and notice* of the fact to the Bank. Unquestionably, as appears from the subsequent letter of O'Flynn and other evidence, Western intended to give and the Bank intended to get an unreasonable advantage over other creditors. This constitutes an intent to 'hinder, delay and defraud' other creditors, and a showing of actual fraud in the sense of gross and corrupt motive is not necessary to be shown. . . .
>
> "The finding of the referee that the Bank did not purchase these lands in good faith must, in view of the authorities and the evidence, be affirmed. . . . .
>
> "The finding of fraudulent intent cuts into clear outline the positions with reference to money expended upon the property by the Bank." (Tr. 207-208)

The testimony on which *lack of consideration* was based came largely from the books and from the testimony of a certified public accountant who examined the same and who testified that he found "no record of any consideration being paid." (Tr. 331-333)

The testimony on which *notice* was based came in part from the attorney for the Bank, Mr. Thos. Greene, and in part from the credit files of

the Bank. The Attorney testified that he had knowledge of the filing of the involuntary petition in bankruptcy against the Western prior to the transactions here involved (Tr. 251) and that the Bank had all the information that he had (Tr. 369-370). And more than that, Exhibit 31, the credit file of the Bank of California, (Tr. 414) shows that under date of 11/28/31 there was entered a memorandum from the Daily Journal of Commerce as follows:

> "Western Bond & Mortgage Company—Involuntary Bankruptcy."

Moreover, in said file there appears a communication addressed "To Bank of California (see its reverse side) from Bradstreet Co. dated May 27, 1931, reporting as follows:

> "Re: Western Bond and Mortgage Co.
>
> "An involuntary petition in bankruptcy was filed in the federal court November 25, 1931, against the above company. Petitioners are: Warren Hardy, Attorney of Seattle, $500.00; D. R. Potter, Prineville, Oregon, $90.00; and Vincent & Vincent, Portland, Oregon, $75.00."

Testimony concerning knowledge by the Bank of the Western's ownership of the Keystone notes and mortgage was supplied by the Attorney for the Bank who had the abstract of title and who examined the same. Asked directly whether he knew that the property on which the Bank was about to take a mortgage was property that the Western held mortgages on at the time, he answered:

> "How could I help knowing it when the abstract showed it. Of course I knew it." (Tr. 267)

Likewise, Mr. Greene testified that he had knowledge of the transfers, satisfactions, mortgages and assignments involved herein (Tr. 256-261). It also appeared from the evidence that the Bank had actual knowledge of the ownership by the Western of all the stock in the Keystone (Exs. 30 and 31, Tr. 413-414). Moreover, Mr. Greene, prior to the filing of the petition in bankruptcy, had heard charges made in a trial against the Western which he attended that the Keystone was a mere dummy of the Western (Tr. 402-404). It also appeared in evidence that the Bank had knowledge of the ownership of all the stock in the Western by the Massachusetts (Tr. 349). It also appears from the testimony that Mr. Greene, the attorney for the Bank, holding in escrow the deed, satisfactions, assignments and mortgages involved in the transaction, must have known the interlocking character of the officers of the various corporations, because in most of the instruments the officers signing them, even when conveying from one corporation to another, were the same.

Lack of good faith is also implicit in the evidence. The very deviousness of the process in itself furnishes an inference from which bad faith may be premised. Judge Fee said:

> "The Bank which obtained this asset, *by whatever devious process*, should be required to return it." (Tr. 205)

And again says Judge Fee:

> "A valuable asset was transferred to the Bank and taken away from Western and its creditors by the *complicated devices* heretofore outlined." (Tr. 206)

Another basis for premising bad faith will be found in a letter written by O'Flynn, President of the Western, to the Bank of California, in reply to a registered letter written by the Bank to Ochoco, care of the Western, demanding the first payment on the note and threatening, unless paid promptly, to declare the whole amount due. O'Flynn interpreted this as a threat to foreclose the mortgage and said:

> "A foreclosure can do nothing but give you the property and prevent any efforts on our part to refinance. In addition thereto might I suggest, and this in all good faith and still in the spirit of co-operation, that such an action might not result favorably for the bank, even though it was successful against the Ochoco Farms Corporation. The bank and the Western Bond are *in rather a delicate position* in this matter and it is not certain but what the plans of both of us might not be upset by the misfortune of a foreclosure. It would seem the part of wisdom as well as good business to wait until the determination of the petition in bankruptcy. The longer this matter is postponed the better the position of the Western Bond and the more probable ratification of all that has been done *in the effort of the Western Bond* to protect this account. At this time and for some little time yet it would seem too big a gamble and risk. . . . . Everything possible has been done by the *Western Bond* and *your attorney* to protect you in the premises and for our part we will continue but naturally might be handicapped if through some action of your own you disturb a present satisfactory condition and *awaken sleeping forces.*" (Ex. 26-a and b, Tr. 317, 319)—Italics ours.
>
> (See Judge Fee's comments on this letter, Tr. 193)

Moreover, in his report to the Home Office of the Bank of California (Ex. 30, Tr. 413) Mr. Alward, its then Portland Manager, explaining why he had set up an account on the Bank's books under the name of "Westco Finance Co.", a fictitious non-existing company, says:

> "This is an unincorporated company set up for convenience in handling the liquidation of assets acquired through the settlement recently made *with the Western Bond & Mortgage Company*. . . . About a year ago it became necessary for us to advance funds for the care of sheep under the mortgages, and it developed that the collateral was entirely inadequate and that a very substantial loss would be faced in liquidation. The Western Bond & Mortgage Company's affairs were not in good shape." (Italics ours.)

And further in the same report Mr. Alward says:

> "The first mortgage on the Ochoco Farms Corporation land is, of course, excessive from the standpoint of a conservative loan. . . . This is the most satisfactory *adjustment* that we could make of a *very bad situation*. . . ." (Italics ours.)

There is a further document in this case which speaks loudly of lack of good faith on the part of the Bank in endeavoring to make it appear that there was acquired property from one detached from the bankrupt. We speak of a contract or bill of sale drafted on behalf of the Bank of California for signature by the Western Bond & Mortgage Company (Trustee's Ex. 22). In that contract under a "Whereas" clause, it is set forth that the Western had pledged to the Bank certain property and that the Bank had accepted said property as security.

Then there is a further "Whereas" clause, as follows:

> "Whereas, to avoid the expense, cost and delay of a suit by the Bank to foreclose its lien upon and sell the said collateral and other securities to apply on said indebtedness, the Company has proposed to convey the same and all its right, title, interest and equity therein and to the properties represented thereby *and other property* to the Bank in full payment and satisfaction of its indebtedness to the Bank, and the Bank is willing to accept the same, *with other property* in full payment of its indebtedness and to surrender and cancel all its claim against the Company in consideration thereof." (Italics ours.)

Then, in consideration of the property turned over to the Bank, the Bank releases its claim against the Western and the Western further "covenants to and with the Bank that it is the lawful owner of said property." The Western, according to the testimony of the Bank's witnesses, was to do nothing. They were to surrender or give no other property than that which it had previously pledged to the Bank. Is it not apparent that the "other property" was property which the Western had at the time of filing the petition in the mortgages upon the Ranch or in the Ranch itself?

We comment on these documents as evidencing the existence of bad faith, by saying *res ipsa loquitur.*

Pomeroy in his work on *Equity Jurisprudence,* Vol. II, Sec. 745, page 205, says:

> "The essential elements which constitute a bona fide purchase are therefore three—a valuable

consideration, the absence of notice and the presence of good faith." (1)

We insist that the evidence showed unquestionably: (1) that the Bank did not pay a valuable consideration in the eyes of the Bankruptcy Law for the property which it acquired;(2) (2) that it did not act without notice; (3) that it did not act in good faith. We unhesitatingly affirm that this Court will not review the two Referees' findings in this regard approved as they were on review and on rehearing by the District Judge.

2. Moneys paid after bankruptcy to another in order to obtain property of the Bankrupt cannot be recovered from the Bankrupt's estate.

(Answering Appellant's Brief pp. 48-50)

In previous portions of this Brief, we have amply shown that the findings of the Referee approved by the Judge were to the effect that the Western received no consideration whatsoever for the property of which it was denuded, and that there was ample evidence on which to base such finding. The record is replete with the fact that the Bank loaned to the Massachusetts $20,000.00 or more on the Massachusetts' own note, covered by collateral security of the Massachusetts, and there is not an iota of evidence that the Massachusetts turned this money over to the Western—in fact, the evidence is to the contrary. In Paragraph IX (Tr. 50) of the Bank's Answer, the Bank states: that a part of the con-

(1) See also Houston Oil Co. v. Wilhelmn (C.C.A. 5th), 182 Fed. 474; Stonebraker-Zea Cattle Co. v. United States (C.C.A. 8th), 220 Fed. 99, 101.

(2) Valuable consideration in bankruptcy means, of course, present consideration and does not include satisfaction of a debt.

sideration for the mortgage which the Bank received was "the advance by Respondent (Bank) *to or for the account of said Massachusetts Mortgage Co. of the sum of* $28,495.71."

Under what equitable theory then can the Bank maintain that it is entitled to receive from the bankrupt estate this money? There are many cases in the books where one in good faith has acquired property and paid to the owner of the property a sum of money and thereafter, through no fault of his own, he has been required to reconvey the property to the former owner. Under such circumstances, many cases hold the original owner is required to return the consideration which he received for the property. We do not quarrel with the cases cited by Appellant on page 49 of its Brief, for they hold nothing more than just stated. But here we have a different situation, even eliminating, (which of course we do not), the question of notice and of bad faith. Here, the Western received *nothing* for its property. We ask, when, in order to obtain a return of property extracted from a trust estate, was it ever held by any court of justice that a beneficiary is required to pay to one who aided in the extraction a sum of money equal to that paid by the abettor to the extractor?

The Appellant also argues in its Brief that since the veil of corporate entity had been pierced in regard to the Keystone and to the advantage of the Western, it should be pierced as to the Western in favor of the Massachusetts. But we an-

swer: there is no evidence in the record that the Western was operating as a mere dummy of the Massachusetts. Only one element requisite for piercing the veil is here present and that is the Massachusetts' ownership of the Western stock. The Western was a separate business entity conducting its own affairs, as was the Massachusetts. At any rate, it is to prevent fraud that corporate entities are pierced, not to perpetuate it. In this instance, we can conceive of no greater injustice than to require a bankrupt estate to take from its creditors funds applicable to their payment for the purpose of rewarding one who paid money to another to assist in obtaining through manipulation, such bankrupt's property.

Moreover, in the answer of the Bank filed to the petition of the Trustee, there is no claim made for repayment of moneys advanced to the Massachusetts.

May we add again that much of the Appellant's Brief in this connection is taken up with the statement based on evidence endeavored to be introduced before Referee Snedecor, which was rejected by him and which rejection was approved by Judge Fee (Tr. 198).

3. **The Bank, being in unlawful possession of the Ranch, will not be allowed credit for alleged permanent improvements since it was not a purchaser in good faith, without notice and for value.**

(Answering Appellant's Brief pp. 51-55)

The question of whether or not the Bank may

obtain a credit for improvements made upon the property after it acquired the same is dependent upon whether or not it was a purchaser for value in good faith and without notice. The law is as Referee Snedecor and Judge Fee held it to be, namely, that it is only a purchaser for value and without notice who can be credited for improvements made upon property which it acquired for value in good faith. We shall not burden the Court with a review of the authorities presented by us before Referee Snedecor and before Judge Fee, and we respectfully refer the Court to that portion of Referee Snedecor's report in which he discusses the law in this regard (Tr. 129-141), and to Judge Fee's opinion (44 Fed. Sup., Advance Sheets No. 1, pp. 89, 94-95, Tr. 208-212), and to the authorities which are discussed and cited in these opinions. This being the law, as we maintain it is, then in view of the finding of notice, absence of valuable consideration and lack of good faith, there can be no crediting of the Bank for such improvements.

We call attention to the fact that Referee Snedecor, with the approval of the parties, made a personal inspection of the Ranch (Tr. 117) and found that

> "These improvements, while adding to the comforts and convenience of operation of the Ranch, added little to its productive value. They are not the type of improvements that would be made by one holding the land for immediate sale; and the Bank knew that if and when the property was restored to the Trustee, it would be the Trustee's duty to sell it for the best price obtainable." (Tr. 142)

Appellant claims it spent "more than $40,586.89 ing rental and other charges" (App. Br. p. 55). However, in its Answer, which remained unamended and unsupplemented, the Appellant claimed that it had

> "Expended for repairs, painting, construction, fences, upkeep, insurance and taxes necessary for the preservation and maintenance of said property the sum of $23,350.51, and has produced hay thereon of the value of $15,560.59, leaving a deficit in operation of $7789.92, which deficit does not include any charge for supervision or accounting or interest upon the investment." (Par. XIII, Tr. 55-56.)

The Court allowed the Bank $9,546.38 (Tr. 226).

4. The order concerning rental value of the Ranch merely fixed the value of the use of the Ranch, against which value allowed credits for advances may be offset; and although the determination be res adjudicata between the parties, it is not a judgment enforceable as such without further court action.

(Answering Appellant's Brief, pp. 56-57)

Under the Oregon statute (*Oregon Compiled Laws Annotated 8-206*) quoted by Appellant in its brief on page 52 where property is unlawfully acquired, the original owner of the property may recover it, together with damages for its use, in lieu of rental, less the value of permanent improvements placed upon the property in good faith. Obviously, upon the endeavor of the Bank to recover for alleged improvements placed upon the property, it was

necessary and proper for the Court to determine the amount of damages (rental value) suffered by the Bankrupt by the deprivation, against which any credit allowed the Bank might be offset. This the Referee did and the Court approved.

The order in this regard may be assimilated to an order of a Referee upon objection disallowing a claim on the ground that the claimant has received a preference. Of course, on such an order, no execution can issue nor by force of the order alone can any recovery be had of the preference, but the order of the Referee is res adjudicata between the parties.(1) And so here, while we admit that no execution may be levied for the recovery of the difference between the rental value as found by the Court and the credit for improvements, nevertheless the order is proper and must be made, certainly where, as here, any credits at all are allowed for advances.

5. Money paid to the Bank for a portion of land sold out of land unlawfully acquired stands in lieu of the land itself, and the turnover order is proper where money is still held.

(Answering Appellant's Brief pp. 58-59)

The testimony will disclose, and it will not be denied, that the Oregon State Highway Commission, in order to obtain a right-of-way over the Ranch for a highway, purchased a portion of the ranch property after bankruptcy from the Bank for the

(1) See Metz v. Knobel (C.C.A. 2nd), 21 Fed. 317, 318; McCulloch v. Davenport Sav. Bank (D.C. Iowa), 226 Fed. 309; Lincoln v. Peoples Nat. Bank (D.C. Mich.), 260 Fed. 422; Clendening v. Red River Valley Nat. Bank, 11 A.B.R. 245, 12 N.D. 51, 94 N.W. 90.

sum of $10,000.00 with the consent of the Trustee, without prejudice to the rights of the respective parties (Tr. Vol. II, p. 478). And it further appears that the Bank made no claim for this $10,000.00 in the event that it was ultimately determined that the Trustee was entitled to the Ranch. See Tr. Vol. II, p. 469, where the following occurs:

> "Mr. Teiser: In addition to that the State paid you $10,000.00?
>
> Mr. Thompson: The $10,000.00 we have intact to your credit to go against whatever allowance you are entitled to get."

Based on these statements, the Referee found (Tr. 128)

> "Shortly after these proceedings were commenced by service on the Bank of an order to show cause . . . . the State of Oregon acquired from the Bank a right-of-way through the Ranch for a new highway. For said right-of-way the State paid the Bank the sum of $10,000.00."

The statement in the Appellant's Brief that the $10,000.00 paid to it was to reimburse it for damages to improvements on the land taken over by the Commission is not borne out by the testimony of the Bank. There is no evidence in the record establishing such claim. Moreover, in this regard, Mr. Thompson said (Tr. Vol. II, p. 469),

> "The pump and engine went together. There were three items the State paid for in addition to the $10,000.00."

See also further remarks of the Referee concerning same (Tr. 128).

Assuming the Trustee is entitled to the Ranch,

as we insist he is, the Trustee's right to the $10,000.00 cannot properly be questioned.

CONCLUSION

We conclude this rather extended Brief with the confident assertion that there is no question of fact here for the Court to review, and that the only questions properly before this Court are those of law, namely: (1) whether or not the Bank acquired *after* the filing of the petition property *of the Bankrupt,* and (2) whether or not improvements and expenditures made by the Bank were of such a nature and made under such circumstances as to entitle the Bank to a credit for the same other than those allowed by the Court. As to these two questions of law, we are equally confident that this Court will not reverse the order of Judge Fee. The conclusions reached, as set forth in his able opinion, reported, as heretofore stated, in 44 Fed. Sup. (Advance Sheets No. 1, p. 89), are we believe unassailable.

Respectfully submitted,

SIDNEY TEISER.

Teiser & Keller.

APPENDIX

APPENDIX

Finding (1)—(Tr. 70)

That on the 25th day of November, 1931, an involuntary petition in bankruptcy was filed in the above-entitled court and cause against the Western Bond & Mortgage Company, an Oregon corporation, and that thereafter on the 24th day of September, 1934, the said Western Bond & Mortgage Company was duly adjudged a bankrupt upon said involuntary petition.

Some of the Supporting Evidence:

"Mr. Teiser: I would like to say at the outset. . . . that it is alleged and admitted in the pleadings that an involuntary petition in bankruptcy was filed. . . and I take it that it is admitted. . . . that there was an order of adjudication. . . .

Mr. Thompson: No question about that." (Tr. 249-250)

See also Petition in Bankruptcy (Tr. 2-4) and Adjudication (Tr. 6)

Finding (2)—(Tr. 71)

That the District Court of the United States for the District of Oregon, where said involuntary petition in bankruptcy was filed, had jurisdiction of the subject matter and of the parties in said bankruptcy proceedings and that the adjudication herein was made after hearing, of which hearing all parties to the proceedings had due notice, and were present, and that said adjudication was a valid order of said court.

Some of the Supporting Evidence:

See Petition in Bankruptcy (Tr. 204); Subpoena (Tr. 5); Return of Service (Tr. 4); and Order of Adjudication and recitals therein (Tr. 6-7).

Finding (3)—(Tr. 71)

That at the time of the filing of said petition in bankruptcy against the Western Bond & Mortgage Company, all the capital stock of the said Western Bond & Mortgage Company was owned by the Massachusetts Mortgage Company, a Washington corporation. . . .

Some of the Supporting Evidence:

"Mr. Teiser: I merely wanted to show that the Western Bond & Mortgage Company was owned and controlled by the Massachusetts Mortgage Co.

Mr. Thompson: We will admit it." (Tr. 269)

See also Exhibit 1 (Tr. 269).

(Testimony of Frederick Greenwood, Manager Portland Branch Bank of California)

"Q. I think you have a statement here that the Massachusetts Mortgage Company owned all of the common stock of the Western Bond & Mortgage Company. You knew that of course, didn't you?

A. Apparently we did, yes." (Tr. 349)

Finding (3) (Continued)

. . . And that the Western Bond & Mortgage Co. was the owner of all of the capital stock of the Keystone Finance Co., an Oregon corporation.

Some of the Supporting Evidence:

(Testimony of Miss E. E. Gallagher, Assistant Secy. and Director of Western Bond & Mortgage Co., also President of the Keystone Finance Co.)

"Q. I hand you affiliations schedule of income tax return for 1930 of the Western Bond and Mortgage Company and ask you whether or not the signatures attached thereto of W. E. Johnson and E. F. O'Flynn attached are the signatures of these people who were officers of the Western Bond and Mortgage Company?

A. Yes, I recognize the signatures of Mr. Johnson and Mr. O'Flynn.

Q. Were they directors of the Western Bond and Mortgage Company?

A. Yes, they were.

Mr. Teiser: I offer this schedule in evidence with the papers attached to it and call particular attention to the item '7' on the schedule and to item '10', one showing the ownership of all the stock in the Central Realty Company by the Western Bond and Mortgage Company, and the other showing the stock of the Keystone Finance Company owned by the Western Bond and Mortgage Company.

. . . . . .

The papers were marked Trustee's Exhibit "7" (Tr. 277-278)

"Q. I hand you certificates numbered four, nine and ten and eleven, Keystone Finance Company, and ask you whether they exhibit correctly the stockholdings of the Keystone Finance Company in February, 1932?

. . . . . .

A. This was all of the stock.

Q. These certificates are signed by you as president, are they not?

A. Three are.

Q. The Western Bond & Mortgage Company cerificate, number four, is signed by whom?

A. E. Hagenbucker and Miss L. Kelly.

Q. Do you know who they are?

A. They were Massachusetts Mortgage Company employees.

Q. They were office employees?

A. I could not say that without looking it up. They were with the Massachusetts Mortgage Company.

. . . . . .

Mr. Teiser: I introduce these four certificates in evidence. They were received and marked as one exhibit, Trustee's Exhibit 14." (Tr. 296-297)

Finding (3) (Continued) (Tr. 71)

. . . . . That said Keystone Finance Company was operated and manipulated at all times by the said Western Bond & Mortgage Company as its adjunct, subsidiary and agent and for the sole purpose of carrying out its designs and biddings, and was a mere corporate shell and had no actual existence for its own purposes, but existed solely as a mere agent and alter ego of the said Western Bond & Mortgage Company.

Some of the Supporting Evidence:

(Testimony of Miss E. E. Gallagher)

"Q. Who were the officers (of the Keystone Finance Company) at that time?

A. I was elected president, B. O'Reilly vice-president and Miss Smith assistant secretary.

. . . . . .

Q. I think you stated that neither you, Miss Smith or Miss O'Reilly owned any stock in this corporation or had any financial interest in it.

A. No, only we were given a qualifying share.

. . . . . .

Q. Who did the stock belong to?

A. I never gave it a thought.

. . . . . .

Q. Mr. Johnson was president of the Western Bond and Mortgage Company for a while, was he not?

A. Yes.

Q. Mr. O'Flynn was a director and an officer of this company before Mr. Johnson resigned, was he not?

A. Yes. . . . Mr. Johnson was president in January, 1931.

Q. Mr. O'Flynn was secretary-treasurer and a director at that time, January 12, 1931?

A. Yes.

Q. And Mr. Johnson and Mr. O'Flynn continued in those offices until May 2, 1932 . . .?

A. Mr. O'Flynn became president when Mr. Johnson resigned.

Q. On what date?

A. May 2, 1932.

. . . . . .

Q. And you were a director of that company, were you not?

A. Yes. . . .

Q. Where was the office of the Keystone Finance Company in February, 1932?

A. At the Western Bond and Mortgage Company.

Q. And for a time previous to that it was there?

A. . . . It was there for some time previous to that time, yes.

Q. Did the Keystone Finance Company pay any rent for its offices during that period of time?

A. Not as far as I know.

Q. You were president, were you not?

A. Yes.

Q. Were you or any of the other officers of that company paid any salary as officers of that company by the Keystone Finance Co.?

A. No.

Q. Your entire compensation came from the Western Bond and Mortgage Co.?

A. You mean our salary.

Q. Yes.

A. Yes.

Q. In other words, you received no compensation from the Keystone Finance Company?

A. No.

Q. Nor did any of the other officers so far as you know?

A. So far as I know. . . . .

Q. Were you and Miss Smith and Miss O'Reilly employees of the Western Bond and Mortgage Company?

A. Yes.

Q. And were there any other employees of the Keystone Finance Company?

A. Not as far as I know.

Q. There was none?

A. No." (Tr. 298-303)

"Q. What positions did Miss Thibodeaux and Miss O'Reilly occupy with the Western Bond and Mortgage Company?

A. They were office employees.

Q. Clerks?

A. Yes.

Q. Stenographers?

A. Yes." (Tr. 294)

"Q. I think you testified you were an office employee of the Western Bond and Mortgage Company and . . . had no financial interest in the company, is that right?

. . . . . .

A. Yes, I was an office employee and had no financial interest in the company. . . .

. . . . . .

Q. When you acted as a director of this company . . . by whom were your actions guided?

A. You mean in the work I did?

Q. No, regarding the action of the board of directors; by whom were your actions governed; who directed you what to do?

A. Mr. O'Flynn.

Q. Did you use your own independent judgment or did you follow his suggestions and requests?

A. No, I thought it was my duty to follow anything Mr. Flynn requested." (Tr. 282-284)

Q. Do you know the purpose for which the Ochoco Farms Corporation was formed . . .?

A. Just as the permit sets forth.

Q. Did Mr. O'Flynn tell you why specifically the corporation was being formed. . . .

A. I can't give any certain words. . . .

. . . . . .

Q. Miss Gallagher, I think you stated the directors and officers of the corporation were you, Miss O'Reilly and Miss Thibodeaux?

A. Yes.

. . . . . .

Q. According to the minutes there, you were president . . . .?

A. Yes.

Q. Miss Thibodeaux was vice-president and assistant secretary?

A. Yes. . .

Q. And Miss B. O'Reilly secretary and treasurer?

A. Yes. . . . .

"Q. In the handling of the books of the Ochoco Farms Corporation, by whose advice and direction were you governed?

A. Mr. O'Flynn and Mr. Johnson.

. . . . . .

Q. You exercised no independent judgment of your own as to what to do?

A. No.

Q. And is that true of Miss Thibodeaux and Miss O'Reilly? Did they also follow the advice and direction of Mr. Johnson and Mr. O'Flynn?
A. Well, I think they did." (Tr. 292-5)

"Q. Did you follow the same course, you and the rest of the parties, Miss Smith and Miss O'Reilly, in regard to your actions as directors (of the Keystone Finance Co.) as you followed in other corporations which you testified to?
A. Yes.
Q. You and the rest of them acted under the directions of Mr. O'Flynn?
A. Yes, and Mr. Johnson." (Tr. 300)

Finding (3) (Continued) (Tr. 71)

That the officers and directors of said three corporations and of the Ochoco Farms Corporation, hereinafter mentioned, were interlocking.

Some of the Supporting Evidence:

(Testimony Miss E. E. Gallagher.)

See diagram of interlocking officers and directors, p. 11 this brief.

Finding (4)—(Tr. 71-73)

That said Keystone Finance Company at the time of the filing of the petition in bankruptcy herein held title in its name to certain real property in the County of Crook, State of Oregon, known as the Russell Ranch, consisting of some eight thousand acres of land and described as follows:

(Here follows the description)

Some of the Supporting Evidence:

See Exhibit 15 (Tr. 304)
See Paragraph II of Trustee's Petition for Order to Show Cause (Tr. 19, 20) and Paragraph II of Answer of Bank to said Petition (Tr. p. 48) admitting ownership of Keystone Finance Co. in the Ranch.

Finding (4) (Continued) (Tr. 73)

. . . . but that said title was held at all times by it for and on behalf of the said Western Bond & Mortgage Company as agent, subsidiary and alter ego of said Western Bond & Mortgage Company.

Some of the Supporting Evidence:

Reference is here made to testimony recited under evidence supporting Finding (3), pp. iv-viii of this Appendix.
See also Exhibit 7 (Tr. 277-8)
See also Exhibit 14 (Tr. 297)

Finding (5)—(Tr. 73)

That at said time of the filing of the petition in bankruptcy herein, the said Western Bond & Mortgage Company was also the owner of two notes, one in the amount of $77,500.00 and the other in the amount of $72,500.00, executed in its favor by the said Keystone Finance Company and secured by first mortgages duly recorded upon the said Russell Ranch in favor of said Western Bond & Mortgage Company, and that said mortgages were first mortgage liens upon said property.

Some of the Supporting Evidence:

See Exhibit 16 (Tr. 304-5)
See admissions in Answer of Bank to Trustee's Petition for Order to Show Cause. (Tr. 48)

Finding (6)—(Tr. 73)

That said Western Bond & Mortgage Company at the time of the filing of said petition in bankruptcy against it was also the owner of twenty bonds of the face value of $500.00 each of Boundary County, Idaho, Drainage District No. 10, bearing interest at 6 per cent per annum.

Some of the Supporting Evidence:

See Exhibits 22 (Tr. 309), 23A (Tr. 313) and 23B (Tr. 314).

(Testimony of Herbert E. Alward, Vice-President and Branch Manager of Bank of California)

"Q. There was involved in that transaction ten thousand dollars par value of bonds of the Kootenai Irrigation District?

A. Yes.

Q. These were negotiable bonds, were they not?

A. Yes.

Q. They were brought to you by the Massachusetts Mortgage Company?

A. Yes." (Tr. 367)

See also supporting testimony under Finding 11, post.

Finding (7)—(Tr. 73-74)

That at the time of the filing of said petition in bankruptcy against said Western Bond & Mortgage Company the said Western Bond & Mortgage Company was indebted to the Bank of California, National Association, a National banking organization duly organized and existing under the National

Banking Act of the United States of America, in an amount upards of $100,000.00, to secure which said Bank of California, National Association, held certain collateral.

Some of the Supporting Evidence:

(*Testimony of R. Erickson*, a Certified Public Accountant)

"Q. There had been loans by the Bank of California to the Western Bond and Mortgage Company of $103,877.96 and accrued interest, from the books?

A. Yes." (Tr. 335)

See also Exhibit 28 (Tr. 340)
See also, Paragraph VII of Bank's Answer and Petition of Trustee to Show Cause, admitting indebtedness to it in the sum of $103,000.00.

(*Testimony of Herbert E. Alward*)

"Q. Did you make efforts that resulted in securing further collateral from the Western Bond and Mortgage Company during the year 1931?

A. Yes.

Q. Tell the court what that was?

A. We secured a deed to some land in Idaho and the assignment of a second mortgage on an apartment house in Seattle, and a number of notes of substantial amount, I have not the figures right in mind, signed by Emery Olmstead secured by some stock. I could tell you a little more about that stock, it was not a very much value." (Tr. 362)

Finding (8)—(Tr. 74)

That on and prior to the 13th day of February, 1932, the said Bank of California, National Associ-

ation, deemed the collateral and security held by it as insufficient to liquidate said indebtedness.

Some of the Supporting Evidence:

Paragraph VIII of Bank's Answer to Trustee's Petition to Show Cause (Tr. 49) admitting such insufficiency.

(*Testimony of Herbert E. Alward*)

"Q. Thereafter what was your attitude and your efforts towards the Western Bond and Mortgage Company and the new management in the way of liquidating their guarantee on paper?

A. We were continuing with every effort to get the sheep loans in better shape, liquidate them where liquidation was possible, and see that they were properly handled to the end that we could realize everything possible out of the sheep that we had loans on." (Tr. 362-3)

Finding (9)—(Tr. 74)

That thereupon and after the filing of the petition in bankruptcy against the said Western Bond & Mortgage Company, the Massachusetts Mortgage Company and the Western Bond & Mortgage Company caused to be formed a corporation named the Ochoco Farms Corporation under the laws of the State of Oregon.

Some of the Supporting Evidence:

See Trustee's Exhibit 9 (Tr. 284)

(*Testimony Miss E. E. Gallagher*)

"Q. Miss Gallagher, I hand you stock certificate book with stubs and blank certificates and stock certificates of the Ochoco Farms Cor-

poration, of which you were president. Will you state whether or not that is the certificate stock book and the issued stock certificates of that corporation, and all of them?

A. Yes, this is a certificate stock book of the Ochoco Farms Corporation.

Q. And the stock certificates issued?

A. And the stock certificates issued.

Q. Is that all of them?

A. Eight hundred and fifty shares.

Q. Are the certificates which I hand to you with the book, all the stock certificates issued of the Ochoco Farms Corporation?

A. Yes.

Q. You say there were eight hundred and fifty shares?

A. Yes.

Q. And that was the entire issued stock of the Ochoco Farms Corporation?

A. Yes.

Mr. Teiser: I introduce in evidence the stock certificates which have been identified as having been issued. (Marked Trustee's Exhibit 10)

. . . . . .

Mr. Teiser: For your information and the information of the Court they were issued one for Miss Thibodeaux, one for Miss O'Reilly, one for Miss Gallagher and 847 to the Massachusetts Mortgage Company. (Tr. 284-5)

Finding (90) (Continued) (Tr. 74)

. . . and caused the Keystone Finance Company

Some of the Supporting Evidence:

See Trustee's Exhibit 19 (Tr. 307)

(*Testimony of Miss E. E. Gallagher*)

"Q. Miss Gallagher, I ask you to look at this minute book identified as Keystone Finance Company's minute book, and ask you whether

or not the first or top sheet is not the record of a special meeting of the board of directors of the Keystone Finance Company . . . February 11, 1932, ...

A. Yes.

Q. Were these minutes signed by you as president and Miss Thibodeaux as secretary?

A. Yes.

Q. Of the Keystone Finance Company?

A. Yes.

Q. Was the office in which the meeting was held at the office of the Western Bond and Mortgage Company?

A. Yes.

. . . . . .

Q. Pursuant to that resolution this deed which I have already introduced, Trustee's Exhibit 18, signed by you and Miss Thibodeaux for the Keystone Fiance Company was executed, is that right?

A. Yes." (Tr. 306-7)

See, also, supporting testimony under Finding (3) pp. iv-viii this Appendix.

Finding (9) (Continued) (Tr. 74)

. . . . to transfer to said Ochoco Farms Corporation title to the said Russell Ranch,

Some of the Supporting Evidence:

See Exhibit 18, deed from Keystone Finance Co. to Ochooc Farms Corporation of the Russell Ranch. (Tr. 305-6)

Finding (9) (Continued) (Tr. 74)

. . . . and simultaneously therewith the Western Bond & Mortgage Company, without receiving any consideration therefor

Some of the Supporting Evidence:

(*Testimony R. Erickson*)

"Q. . . . . I will ask you whether or not the books show that the Western Bond and Mortgage Company received any consideration from the Keystone Finance Company for the satisfaction of these mortgages?

A. The Western Bond and Mortgage Company received nothing from the Keystone Finance Company to satisfy either of these mortgages." (Tr. 332)

Finding (9) (Continued) (Tr. 74)

. . . . released and satisfied the said mortgages which it held against said property, thus giving to the Ochoco Farms Corporation the fee simple title to the said Russell Ranch unencumbered by any mortgage liens whatsoever.

Some of the Supporting Evidence:

See Trustee's Exhibit 17, satisfaction of mortgages from the Western Bond & Mortgage Company to the Keystone Finance Co. (Tr. 305)

Finding (9) (Continued) (Tr. 74-5)

That thereupon the Ochoco Farms Corporation executed and delivered to the Massachusetts Mortgage Company a first mortgage upon said Russell Ranch to secure notes aggregating $55,960.00, thereby supplanting the first mortgages theretofore held by the Western Bond & Mortgage Company.

Some of the Supporting Evidence:

See Exhibit 20, mortgage from Ochoco Farms Corporation to the Massachusetts Mortgage Company (Tr. 307)

Finding (9) (Continued) (Tr. 75)

That the said Massachusetts Mortgage Company thereupon simultaneously assigned said notes, aggregating $55,960.00, and the mortgage securing the same to the Bank of California, National Association.

Some of the Supporting Evidence:

See Exhibit 21, assignment of mortgage from Massachusetts Mortgage Company to the Bank of California (Tr. 308)

Finding (10)—(Tr. 75)

That the amount of the notes assigned to the Bank of California, National Association, secured by the mortgage, likewise assigned, was the aggregate of advances theretofore made by the Bank of California, National Association, to the Massachusetts Mortgage Company and the amount of the debt owing by the Western Bond & Mortgage Company, after computing and giving credit to the Western Bond & Mortgage Company for the value of the securities already held by the Bank.

Some of the Supporting Evidence:

See Exhibit 28 (Tr. 340) and Exhibit 30 (Tr...

(*Testimony of R. Erickson*)

"Q. Explain from what you got this information you refer to; what it was.

A. In the files of the Ochoco Farms Corporation there is a memorandum showing the details of the settlement, and I think the notation shows as per Mr. Greenwood's figures of February 17, 1932.

. . . . . .

A. Yes, they are part of the items that make up the $28,495.71 which added to $27,464.29 amount to $55,960.00." (Tr. 334-7)

"Q. Mr. Erickson, you prepared a memorandum from which you testified yesterday of certain figures.

A. Yes.

Mr. Teiser: Is there any objection to having this marked as an exhibit merely for the purpose of giving to the court the figures more easily, but not for probity, just so the court may have before it the tabulation in understandable form? Is there any objection to that?

Mr. Thompson: No objection to be used to illustrate his testimony.

The paper was introduced and marked Trustee's Exhibit 28." (Tr. 340)

Finding (10) (Continued) (Tr. 75)

. . . . . that upon receiving the assignment of said notes and mortgage securing same, the Bank of California, National Association, returned to the Massachusetts Mortgage Company the collateral belonging to the Massachusetts Mortgage Company which the Bank held as security for said advances.

Some of the Supporting Evidence:

(*Testimony of Frederick Greenwood,* Branch Manager of The Bank of California)

"Q. And as a matter of fact that collateral was returned when you accepted the assignment of the mortgage?

A. It was." Tr. 345)

Finding (10) (Continued) (Tr. 75)

. . . . and which was deemed by the Bank sufficient to protect the Bank for said advances made

by it to said Massachusetts Mortgage Company.

Some of the Supporting Evidence:

(*Testimony Frederick Greenwood*)

"Q. I understand then that the collateral, plus the financial statement of the Insurance Building Corporation and the financial statement of the Massachusetts Mortgage Company and the notes placed as security for these two notes, would to your mind be ample security and be responsible for the payment of these two notes?

A. We regarded that collateral as protecting us temporarily until the transaction could be accomplished." (Tr. 348)

Finding (10) (Continued) (Tr. 75)

. . . . and also released the debt then owing by the Western Bond & Mortgage Company to it.

Some of the Supporting Evidence:

See Exhibit 22 (Tr. 309)

(*Testimony of Thomas G. Greene,* Attorney for the Bank)

"A. . . . Mr. O'Flynn then wanted a memorandum in the form of a bill of sale, or otherwise, showing complete release and discharge of the Bank of California of its claim against the Western Bond and Mortgage Company . . . and in pursuance of his request I prepared this draft of bill of sale, and also a release of the Bank's claim against the Western Bond and Mortgage Company . . O'Flynn wanted it and he wanted a specific stipulation that the Western Bond and Mortgage Company was released and discharged of its liability on its endorsement on that paper." (Tr. 396-7)

Finding (11)—(Tr. 75-76)

That as a part of the same transaction, the Western Bond & Mortgage Company also transferred to the Bank of California, National Association, or caused to be transferred to it, twenty certain Idaho Irrigation Bonds of the face value of $500.00 each, issued by Boundary County, Idaho, Drainage District No. 10, which bonds were at the time of the filing of the petition in bankruptcy the property of the Western Bond & Mortgage Company.

Some of the Supporting Evidence:

See Exhibit 22 (Tr. 309), Exhibit 23-A (Tr. 313) and Exhibit 23-B (Tr. 314).

(*Testimony of Miss E. E. Gallagher*)

"Q. Miss Gallagher, I hand you the journal of the Western Bond and Mortgage Company, showing journal entry 51583, together with the paper attached, and ask you if that is a part of the journal entries of the Western Bond and Mortgage Company?

A. Yes, that is the journal.

. . . . . .

That is in reference to the Kootenai bonds.

. . . . . .

Q. Miss Gallagher, I ask you whether or not in the files of the Western Bond and Mortgage Company there was a receipt which I have handed you?

A. Yes.

Q. Was that signed by the Western Bond and Mortgage Company?

A. Yes.

Q. That is a receipt for the Kootenai bonds from the Ochoco, as transferred from the Ochoco by O'Flynn, a receipt by O'Flynn for the

bonds which had been transferred from the Ochoco.

A. Yes.

. . . . . .

Q. Will you interpret it?

A. 'Sold Ochoco Farms Corp. 1000, they pledge them with Bank of California.'" (Tr. 309, 311-12)

See Paragraph X Trustee's petition (Tr. 25-6) and Bank's answer thereto (Tr. 51).

Finding (12)—(Tr. 76)

That (a) the said deed to the Ranch property from the Keystone Finance Company to the Ochoco Farms Corporation, (b) the said release and satisfaction of mortgages by the Western Bond & Mortgage Company to the Keystone Finance Company, (c) the said mortgage securing notes for $55,960.00 from the Ochoco Farms Corporation to the Massachusetts Mortgage Company, and (d) the assignment of mortgage, securing said notes, from the Massachusetts Mortgage Company to the Bank of California, National Association, were all simultaneously caused to be recorded on the County Records of Crook County, Oregon, on March 2, 1932, by the attorney for the Bank of California, National Association, to whom all of said instruments had been delivered, and who was holding the same in escrow, awaiting the determination by the Bank as to the sufficiency of the value of Russell Ranch adequately to secure the notes of $55,960.00.

Some of the Supporting Evidence:

See Exhibit 24 (Tr. 26).

(*Testimony Thos. G. Greene*)

"Q. Were these papers recorded by you at the same time and returned to you?

A. They were; they were delivered to me by some representative of the Massachusetts Mortgage Company, probably Mr. O'Flynn, and I sent the whole bunch to the clerk of Crook County, and that is the way my name came to be stamped on the bottom of the original, Return to the office of Thomas G. Greene, instead of the Western Bond and Mortgage Company . . . ." (Tr. 415)

Finding (13)—(Tr. 76-77)

That as a result of the assignment of the mortgage securing said notes in the amount of $55,960.00 the said Bank became the possessor of said notes and mortgage and that the said Bank upon the receipt of said notes and the recordation of the assignment of mortgage securing the notes of $55,960.00 released the Western Bond & Mortgage Company from the indebtedness which it owed said Bank,

Some of the Supporting Evidence:

See Trustee's Exhibit 22. (Tr. 309)
See Paragraph IX of Bank's Answer to Trustee's Petition to Show Cause (Tr. 49, 50) admitting that it became possessed of said notes and mortgage.

(*Testimony of Thomas G. Greene, Attorney for the Bank*)

"A. . . . . Mr. O'Flynn then wanted a memorandum in the form of a bill of sale, or otherwise, showing complete release and discharge

by the Bank of California of its claims against the Western Bond and Mortgage Company . . . and in pursuance of his request I prepared this draft of bill of sale, and also a release of the Bank's claim against the Western Bond and Mortgage Company . . . O'Flynn wanted it and he wanted a specific stipulation that the Western Bond and Mortgage Company was released and discharged of its liability on its endorsement on that paper." (Tr. 396-7)

Finding (13) (Continued)—(Tr. 77)

. . . . and that the Western Bond & Mortgage Company received no other or further consideration from said Bank or from others.

Some of the Supporting Evidence:

(*Testimony of R. Erickson*)

"Q. . . . . I will ask you whether or not the books show that the Western Bond and Mortgage Company received any consideration from the Keystone Finance Company for the satisfaction of these mortgages?

A. The Western Bond and Mortgage Company received nothing from the Keystone Finance Company to satisfy either of these mortgages.

. . . . . .

Q. You found no record of any consideration being paid?

A. No record of any consideration being paid." (Tr. 331-333)

Finding (14)—(Tr. 77)

That after the notes secured by said mortgage assigned to the said Bank of California, National Association, became due, the said Bank of California, National Association, foreclosed the said mort-

gage and upon foreclosure sale, bid in the said Russell Ranch at Sheriff's sale held on the 1st day of December, 1933, for $64,328.30 and at the same time bid in the twenty Boundary County, Idaho, Drainage District No. 10 bonds, foreclosed at the same time, for the sum of $500.00 and received delivery of said bonds; and that thereafter, the said Bank of California, National Association, received a Sheriff's deed for the said Russell Ranch.

Some of the Supporting Evidence:

See Paragraph XII of Trustee's amended petition for order to show cause (Tr. 27-8) and Paragraph XII of Bank's answer to said petition (Tr. 52-55).

Finding (15)—(Tr. 77)

That the said Bank of California, National Association, ever since December 1, 1933, had and now has possession of said bonds and of said Russell Ranch.

Some of the Supporting Evidence:

Same as Finding (14) above.

Finding (16)—(Tr. 77)

That the Bank of California, National Association, had actual knowledge, prior to the receipt of the notes aggregating $55,960.00 and prior to the assignment of mortgage to it securing said notes and prior to the executing and recordation of the instruments referred to in Finding No. 12, of the filing of the petition in bankruptcy against the Western Bond & Mortgage Company,

Some of the Supporting Evidence:

(*Testimony Thomas G. Greene*)

"Q. You were attorney for that bank when the transactions with the Western Bond and Mortgage Company and the Massachusetts Mortgage Company were negotiated which is the subject of inquiry today?

A. Yes.

Q. You were attorney for them in February, 1932?

A. Yes.

Q. Will you state whether or not at the time you were attorney for the Bank in this connection in February, 1932, and at the time these negotiations were initiated and negotiated you had knowledge of the fact that the Western Bond and Mortgage Company had an involuntary petition in bankruptcy filed against it?"

. . . . . .

Certainly I did." . . . (Tr. 251)

(*Testimony of Herbert E. Alward*)

"Q. And he was your representative in the matter?

A. Mr. Greene at that time and since has been the attorney we have used when we have needed legal advice and assistance.

Q. And whatever information he had you were satisfied to take?

. . . . . .

Mr. Greene: They had all the information I had." (Tr. 369-370)

See also Trustee's Exhibit 31 (Tr. 414).

Finding (16) (Continued) (Tr. 77-78)

. . . . and had actual knowledge at and prior to said time of the ownership by the Western Bond & Mortgage Company of the notes given by the Key-

stone Finance Company in the amount of $77,500.00 and of $72,500.00, and of the ownership of the two first lien mortgages upon the said Russell Ranch to secure the payment of said notes, and of the recordation thereof; and that said Bank, also at said time, had knowledge of the fact that the recordation of the satisfaction of the mortgages held by the Western Bond & Mortgage Company and the recordation of the mortgage to the Msasachusetts Company and the recordation of the assignment of that mortgage to it would supplant in its favor the first mortgage lien held by the said Western Bond & Mortgage Company upon said Russell Ranch, and accordingly would deprive the Western Bond & Mortgage Company of its property rights in said Ranch;

Some of the Supporting Evidence:

See Exhibits 24 and 25 (Tr. 261)

(*Testimony of Thomas G. Greene*)

"Q. You did know that the property that you were about to take a mortgage on was property that the Western Bond and Mortgage Company held mortgages on at the same time?

A. How could I help knowing it when the abstract showed it. Of course I knew it. . . . (Tr. 267)

Q. Mr. Greene, when you examined this title —you did examine the title, did you not?

A. I examined the title.

Q. As to the Russell Ranch?

A. Yes.

. . . . . .

Q. Before the assignment was taken you

had the abstract before you?

A. Yes.

Q. And at that time, . . . there appears to be recitation of the facts that the Keystone Finance Company, an Oregon corporation, had executed a mortgage to the Western Bond and Mortgage Company for seventy-two thousand five hundred dollars, and another mortgage from the Keystone Finance Company . . . for seventy-seven thousand five hundred dollars . . . . . ?

A. That is correct.

Q. And that was apparent in the abstract?

A. It was.

. . . . . .

Q. The abstract also showed, ... did it not, that under date of February 13, 1932, these two mortgages had been satisfied by two satisfactions of mortgages, dated as I said, February 13, 1932, and recorded March 2, 1932?

. . . . . .

A. . . . . I know, as a matter of fact, that was done, I saw the resolution.

. . . . . .

Q. The abstract also shows a deed from the Keystone Finance Company, an Oregon corporation, to the Ochoco Farms Corporation, dated February 13th and recorded March 2, 1932, of the property covered by the mortgages and the satisfactions of mortgage; is that right?

A. Yes. . . . That is what it shows." (Tr. 256-9)

"Q. There is also shown in this abstract a mortgage from the Ochoco Farms Corporation to the Massachusetts Mortgage Company upon the same property, the Russell Ranch, to secure a note of $55,960.00 which was dated February 13, 1932,, and filed and recorded on March 2, 1932?

A. Yes that appears to be in there also, and

I think I saw that too before it was put on record." (Tr. 260-1)

"A. My recollection is these instruments were delivered at the same time; they were executed at different dates. The execution of the assignment of the Massachusetts Mortgage Company to the Bank of California was subsequent." (Tr. 259)

Finding (16) (Continued) (Tr. 78)

. . . . and that the said Bank also had actual knowledge of the true character of the Keystone Finance Company in relation to the said Western Bond & Mortgage Company as set forth in Finding No. 3;

Some of the Supporting Evidence:

See Exhibit 30 (Tr. 413)
See Exhibit 31 (Tr. 414)

(*Testimony of Thomas G. Greene*)

"Q. You say you went up to the court to hear these lawsuits?

A. I did not hear any of the suits. I heard arguments.

Q. Did you examine the papers in the cases at all?

A. Some I did. . . .

The Court: Where were these suits you refer to?

A. One was commenced in March, 1931, and the other one in April, 1931, the principal one I think. There were four or five others.

. . . . . .

Q. Why did you go up to hear the arguments?

. . . . . .

A. Because the Bank of California was trying to get some additional security from the Western Bond and Mortgage Company.

Q. Did you know of this suit against the Western Bond and Mortgage Company brought by Allen McCurtain?

A. Yes, that was one of them.

Q. And another brought by Carl Little?

A. Yes.

Q. And the John Brocker suit brought in the United States District Court?

A. Yes.

. . . . . .

Q. Don't you know that the charge was made in that suit that the Keystone Finance Company was a mere dummy of the Western Bond and Mortgage Company?

A. I didn't know it was charged in the complaint. I heard it, I think from some lawyer up there." (Tr. 402-4)

Finding (16) (Continued) (Tr. 78)

. . . . and of the ownership by the Massachusetts Mortgage Company of all of the stock in the Western Bond & Mortgage Company.

Some of the Supporting Evidence:

(*Testimony of Mr. Greenwood*)

"Q. I think you have a statement here that the Massachusetts Mortgage Company owned all of the common stock of the Western Bond and Mortgage Company. You knew that of course, didn't you?

A. Apparently we did, yes." (Tr. 349)

Finding (16) (Continued) (Tr. 78)

. . . . and of the interlocking character of the officers of the various companies, as also set forth in Findings No. 3.

Some of the Supporting Evidence:

See various instruments filed as Exhibits in this cause bearing the signatures of the identical individuals as officers of the various companies, all of which were held by Mr. Greene under escrow and which were recorded by him.

Finding (17)—(Tr. 78-79)

That as a result of the transactions heretofore detailed the said Western Bond & Mortgage Company, and the estate in bankruptcy thereof, after the filing of the petition in bankruptcy herein, was depleted of its property in the said Russell Ranch and of its first mortgage liens thereon, and of its property in said $10,000.00 par value Boundary County, Idaho, Drainage District No. 10 Bonds.

Some of the Supporting Evidence:

See as to the fact that the Bank of California obtained the Russell Ranch and the bonds, admissions in Paragraph XI of the Bank's Answer to trustee's petition for order to show cause, wherein it is said:

". . . . and further answering the same says that . . . . the *acceptances by respondent* for a valuable consideration *of the assets hereinabove mentioned* . . . ." (Tr. 51-2)

And as to the depletion phase of this finding, see testimony of Certified Public Accountant, Erickson, set forth in supporting evidence under Finding 13 (continued) to the effect that the books showed no consideration received by the Western Bond & Mortgage Company for the transfer or relinquishment of its interest in these properties.

Also see Diagram, p. 13 of this brief.

Finding (18)—(Tr. 79)

That the value of said Russell Ranch on December 1, 1933, the time said Bank of California, National Association, obtained possession thereof, was $65,000.00.

Some of the Supporting Evidence:

(*Testimony of Frederick Greenwood*)

"We had an inspection made of the Russell Ranch, ... and ascertained the reasonable value of that property." (Tr. 344)

(*Testimony of William Kennedy,* specialist in property management and appraisements.)

"Q. Did you at the request of the Bank of California make an appraisement of what is known as the Russell Ranch in eastern Oregon in December, 1930 or January, 1931?

. . . . . .

A. As I recall it now it was in January, 1932.

. . . . . .

Q. What valuation did you put on it?

A. I valued it at from $64,500.00 to $65,000.00." (Tr. 386)

Finding (18) (Continued) (Tr. 79)

. . . . and that the value of the said Drainage District Bonds on December 1, 1933, when said Bank of California, National Association, obtained possession of them, was $1,000.00.

Some of the Supporting Evidence:

See Paragraph XIII of the Bank's answer to trustee's petition for order to show cause, wherein it is said:

". . . . and denies that the value of said Drainage District Bonds on or about February 13, 1932, was $5,000.00, or any other or greater sum than $1,000.00 . . . ." (Tr. 55)

Finding (19)—(Tr. 79)

That the estate in bankruptcy of the Western Bond & Mortgage Company was diminished to the extent of the value of said Russell Ranch and of the value of said Bonds and that said diminution occurred after the filing of the petition in bankruptcy to the knowledge of the Bank of California, National Association.

Some of the Supporting Evidence:

See supporting evidence to Finding (17).

Finding (20)—(Tr. 79)

That no present consideration, fair or otherwise, was paid by the Bank of California, National Association, for the said Russell Ranch or for the said Drainage District Bonds.

See Certified Public Accountant Erickson's testimony under supporting evidence to Finding 13 (continued), p. xxii this Appendix.

Finding (21)—(Tr. 79)

That said transactions in relation to said Russell Ranch and to said Drainage District Bonds was a transaction out of the ordinary course of business of said Western Bond & Mortgage Company and of said Bank of California, National Association.

Some of the Supporting Evidence:

See report of Mr. Alward to the Home Office of the Bank, Exhibit 30 (Tr. 413) and see letters Exhibit 29 (Tr. 379).

The fact that the transaction was carried on the books of the Bank under the heading "Westco Finance Co." (Tr. 380-1)